

**COMPREHENSIVE
ANNUAL FINANCIAL REPORT
CITY OF ADRIAN, MICHIGAN
DEPARTMENT OF FINANCE**

For Fiscal Year Ended June 30, 2004

Prepared by the Finance Department

JEFFREY C. PARDEE, C.P.F.O., Director of Finance

CINDY L. PRUE, Assistant Director of Finance

AUDITING PROCEDURES REPORT

Issued under P.A. 2 of 1968, as amended. Filing is mandatory.

Local Government Type <input checked="" type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input type="checkbox"/> Other		Local Government Name CITY OF ADRIAN, MICHIGAN	County LENAWEE
Audit Date JUNE 30, 2004	Opinion Date AUGUST 6, 2004	Date Accountant Report Submitted to State: OCTOBER 20, 2004	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan by the Michigan Department of Treasury.

We affirm that:

1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

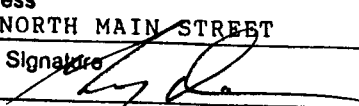
We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- ☐ yes ☒ no 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☐ yes ☒ no 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☐ yes ☒ no 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ yes ☒ no 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ yes ☒ no 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☐ yes ☒ no 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ yes ☒ no 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ yes ☒ no 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ yes ☒ no 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

We have enclosed the following:

	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	X		
Reports on individual federal financial assistance programs (program audits).			X
Single Audit Reports (ASLGU).	X		

Certified Public Accountant (Firm Name) ROBERTSON, EATON & OWEN, P.C.			
Street Address 121 NORTH MAIN STREET	City ADRIAN	State MI	ZIP 49221
Accountant Signature 			

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Finance Department

100 E. Church St. • Adrian, Michigan 49221-2773

(517) 263-2161 • Fax (517) 265-8133

COMPREHENSIVE ANNUAL FINANCIAL STATEMENT

Transmittal Letter

October 18, 2004

To the Citizens of the CITY OF ADRIAN, MICHIGAN,
Honorable Mayor and Members of the City Commission:

Michigan State law requires that all general-purpose local governments publish within six months of the close of each fiscal year a complete set of financial statements presented in conformity with generally accepted accounting principles (GAAP) and audited in accordance with generally accepted auditing standards by a firm of licensed certified public accountants. Pursuant to that requirement, we hereby issue the comprehensive annual financial report of the CITY OF ADRIAN for the fiscal year ended June 30, 2004.

In June 1999, the Governmental Accounting Standards Board (GASB) adopted Statement Number 34, *Basic Financial Statements – and Management’s Discussion and Analysis – For State and Local Governments*. This new accounting pronouncement has a substantial impact on both the format and content of the information included in this report, the second Comprehensive Annual Financial Report prepared under the requirements of the new reporting model. Tom Allen, GASB Chairman stated, “This is the most significant change to occur in the history of governmental financial reporting.”

The new financial reporting model requires general-purpose governments to present the following basic financial statements and Required Supplementary Information (RSI) in order for the financial statements to be in conformance with generally accepted accounting principles (GAAP):

- Management’s Discussion and Analysis (MD&A)
- Government-wide Financial Statements
- Fund Financial Statements
- Notes to the Financial Statements
- Required Supplementary Information (RSI)
- In addition, the State of Michigan requires that individual fund columns be presented for all funds and component units.

The new financial statement includes a discussion of the City's financial condition and outlook. The new *Management Discussion and Analysis* (MD&A) precedes the full-accrual "*Government-wide Financial Statements*" that are intended to show whether today's taxpayers have paid the full cost of the services received. These full-accrual statements are followed by a revised version of the financial statements previously reported, "*Fund Financial Statements*", which report governmental activities on the "modified accrual" basis of accounting, followed by *Footnote Disclosures* and *Required Supplementary Information* (RSI).

The financial statements include several tiers of information, some of which are familiar and some of which are new. The MD&A, a narrative discussion preceding the government-wide financial statements, will analyze:

- The City's financial performance for the year
- A comparison of the current year to the prior year
- A discussion of whether the City's financial position has improved or deteriorated during the year
- Significant changes in individual funds
- Significant budget variances
- A brief explanation of capital asset and long term debt activity
- Any likely future significant changes in financial position or operating results.

The second tier of information includes the two new full-accrual "*government-wide*" financial statements prepared using the economic resources measurement focus; the **Statement of Net Assets** and the **Statement of Activities**. These government-wide financial statements now include all capital assets, including infrastructure, as well as the cost of asset purchases over the years they are in service (i.e., depreciation). These statements also include all long-term liabilities, including employee compensated absences. Compensated absences are recognized as expenses in the year that the employees' services are rendered, since this is when the employees earn them. For example, governments are now required to charge the cost of employee benefits, including sick and vacation pay, over the years that employees are rendering services (rather than decades later, when those benefits are typically paid).

The financial statements maintain some familiarity in the third tier, the "Fund" financial statements. The traditional modified accrual reporting of individual governmental funds has been retained. The GASB believes that this is the preferable method to show budgetary accountability.

Significant individual funds (referred to as "Major" funds) are presented separately on the statements preceding the footnotes. The fund-based statements are separated into three sections:

- governmental funds
- proprietary funds (e.g., water and waste water funds), and
- fiduciary funds (e.g., Agency Fund).

The government-wide and fund financial statements continue to require various note disclosures to supplement the basic financial statements.

Required Supplementary Information (RSI), presented after the notes to the financial statements, include budgetary comparison schedules for the debt service and non-major special revenue funds (e.g., Community Development Fund). Budget to actual comparisons include the original budget, as well as the final amended budget.

The Comprehensive Annual Financial Report consists of management's representations concerning the finances of the City of Adrian. Consequently, management assumes full responsibility for the completeness and reliability of all of the information presented in this report. To provide a reasonable basis for making these representations, management of the City of Adrian has established a comprehensive internal control framework that is designed to both protect the government's assets from loss, theft or misuse and to compile sufficient reliable information for the preparation of the City of Adrian's financial statements in conformity with GAAP. Because the cost of internal controls should not outweigh their benefits, the City of Adrian's comprehensive framework of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatement. As management, we assert that, to the best of our knowledge and belief, this financial report is complete and reliable in all material respects.

The City of Adrian's financial statements have been audited by Robertson, Eaton & Owen, P.C., a firm of licensed certified public accountants. The goal of the independent audit was to provide reasonable assurance that the financial statements of the City of Adrian for the fiscal year ended June 30, 2004, are free from material misstatement. The independent audit involved examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; assessing the accounting principles used and significant

estimates made by management; and evaluating the overall financial statement presentation. The independent auditor concluded, based upon the audit, that there was a reasonable basis for rendering an unqualified opinion that the City of Adrian's financial statements for the fiscal year ended June 30, 2004, are fairly presented as the first component of the financial section of this report.

The independent audit of the financial statements of the City of Adrian was part of a broader, federally mandated "Single Audit" designed to meet the special needs of federal grantor agencies. The standards governing Single Audit engagements require the independent auditor to report not only on the fair presentation of the financial statements, but also on the audited government's internal controls and compliance with legal requirements, with special emphasis on internal controls and legal requirements involving the administration of federal awards. The Single Audit Report is an integral part of this Comprehensive Annual Report (Reference pages 127-129).

GAAP require that management provide a narrative introduction, overview and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The City of Adrian's MD&A can be found immediately following the report of the independent auditors.

Profile of the Government

The City of Adrian, founded in 1825, incorporated in 1853 and re-chartered in 1957, is the county seat of Lenawee County, one of the richest agricultural counties in Michigan. The population of the City of Adrian in 2000 was 22,215, with moderate growth in population since then. Adrian is located 33 miles northwest of Toledo, Ohio, 37 miles south of Ann Arbor and 59 miles southwest of Detroit, and is served by Michigan highways US223, M52 and M34. The City of Adrian is empowered to levy a property tax on both real and personal properties located within its boundaries. The City is also empowered by state statute to extend its corporate limits by annexation, which occurs periodically when deemed appropriate by the City Commission, in accordance with the rules and regulations of the State Boundary Commission. In recent years the City boundaries have expanded through annexation by 1.2 square miles, from 6.9 square miles to 8.1 square miles.

The City of Adrian has operated under the commission-administrator form of government since 1957. Policy-making and legislative authority are vested in a governing commission consisting of the mayor and six other members elected at-large on a non-partisan basis. The City Commission is responsible, among other things, for passing ordinances, adopting the budget, appointing committees, and hiring both the government's administrator and attorney. The City Administrator is responsible for carrying out the policies and ordinances of the City Commission, for overseeing the day-to-day operations of the government, and for appointing the heads of the various departments. Commission members serve four-year staggered terms, with three Commission members elected every two years. The mayor is elected to serve a two-year term.

The City of Adrian provides a full range of services, including police and fire protection, sanitation services, construction and maintenance of highways, streets and other infrastructure, Dial-A-Ride transportation and Community Development services and recreational activities and cultural events. In addition to general government activities, the City Commission is financially responsible for the activities of the water and sewer systems, the City of Adrian Building Authority, a blended component unit, therefore, its activities are included as an integral part of the reporting entity. Also included in the City's financial report are the Downtown Development Authority and the Local Development Finance Authority as discreetly presented component units. However, the Adrian Board of Education and the Bixby Medical Center have not met the established criteria for inclusion in the reporting entity and, accordingly, are excluded from the financial report.

FACTORS AFFECTING FINANCIAL CONDITION

The annual budget serves as the foundation for the City of Adrian's financial planning and control. All departments of the City government are required to submit requests for appropriation to the City's Chief Fiscal Officer on or before the last Tuesday in February each year. The City Administrator uses these requests as the starting point for developing a proposed budget. The Recommended Budget is presented to the City Commission for consideration at the first Commission Meeting in April. The Commission is required to hold a public hearing on the proposed budget and to adopt a final budget by no later than the Commission's second meeting in May. The appropriated budget is prepared by fund (General Fund), department (Parks and Recreation) and activity (Swimming Pool). Transfers of appropriations within and between departments require the special approval of the City Commission in the form of a budget amendment. Budget-to-actual comparisons are

provided in this report for each individual governmental fund for which an appropriated annual budget has been adopted. For the General Fund, Major and Local Street Funds, these comparisons are provided on Pages 41-45 as part of the basic financial statements for the governmental funds. For governmental funds, other than the general fund, with appropriated annual budgets, this comparison is presented in the governmental fund subsection of this report, which starts on Page 82.

On the November, 2003 General Election Ballot, there was a question regarding the detachment of City of Adrian properties to the Charter Township of Adrian. The taxable value of the subject properties approximates \$5.1 million and would generate about \$69,000 in additional tax revenue. Since these properties were recently annexed by the City of Adrian and subsequently called into question, they remained on the Charter Township of Adrian assessment and tax rolls until the issue was resolved by a majority vote reaffirming the previous annexation. The taxable value of the subject properties will transfer from the Township to the City, beginning with the 2004 Assessment Roll and reflect in the FY2004-05 Tax Roll.

The information presented in the financial statements is perhaps best understood when it is considered from the broader perspective of the specific environment within which the City of Adrian operates.

ECONOMIC OUTLOOK

National Economy - Between 1991 and 2001, the U.S. economy enjoyed its longest expansion of the post-World War II era. According to the National Bureau of Economic Research – which is widely acknowledged as the arbiter of business cycle dating – that expansion ended in March 2001 and the economy entered a recession.

By historical standards, this recession was mild, both in terms of its duration and its effect on total output. The recession ended in November 2001, just eight months after it began. And real Gross Domestic Product (GDP) contracted only 0.6 percent between its peak and trough, about one-fourth the average decline in every other recession since 1960.

During this time, low interest rates helped keep sales of light vehicles and homes relatively strong, even though both normally drop off sharply during an economic slowdown. As a result, real household spending continued to expand and that, in turn, cushioned the decline in GDP.

However the recovery, throughout 2002 and into 2003, failed to gain momentum because of a string of unique shocks to economic activity and business decision making. First, were the events of September 11, 2001 and the start of the war on terrorism. Second, were the revelations of corporate malfeasance and the changing environment of corporate governance.

All things considered, the economy has not performed too shabbily so far in 2004. Growth in the first quarter exceeded 4 percent for the third consecutive quarter and averaged a sturdy 5.5 percent over the last three quarters. That's the fastest three-quarter pace since 1984, which should erase the subpar label given to this recovery over its first eighteen months.

One of the defining qualities of the current recovery is the sluggish growth in jobs. Despite the creation of over a million jobs this year and nearly 1 ½ million over the past twelve months, the increase in payrolls has lagged past recoveries by a considerable margin. Indeed, only recently have more people held jobs that at the end of the recession, and even now the improvement is negligible. In June, for example, the number of workers drawing paychecks from non-farm companies stood a mere 0.3 percent above the level that prevailed at the end of the recession in November, 2001.

That's in sharp contrast to the 7.5 percent average gain in payrolls that normally occurs at this stage of a recovery. Of the six upturns since the early 1950s that lasted at least 31 months – the length of the current recovery so far – the increases ranged from a high of 9.8 percent to a low of 2.9 percent. Had the current recovery generated the same percentage increase in jobs as the average, there would now be about 9 million more workers on payrolls. That shortfall goes a long way towards explaining why the current recovery has been far weaker than past ones.

Simply put, the potential income that could have entered the spending stream was never earned. The dollar amounts are huge. In 2003, wages and salaries totaled \$5.1 trillion spread over 130 million non-farm workers, which averages out to \$39,260 per worker. Had 9 million more jobs been created over the past 31 months drawing the average salary, households would have received an additional \$350 billion in incomes. Even if they spent only half of that amount, economic growth would have been boosted by about half a percentage point each year. That would have lifted the average growth rate during the current recovery from 3.6 percent to 4.1 percent, putting it squarely in line with past upturns.

To be fair, that simple math does not take into account offsetting positive influences, which would not have been present had job creation lived up to past recoveries. Most significantly, with employment declining for an unprecedented 20 months following the recession's end, the Federal Reserve embarked on the most aggressive campaign in modern history to stimulate growth and thwart a potential deflation threat. As a result, interest rates were driven down to levels not seen in nearly five decades, and remained there for a far longer period than is customary during a recovery.

This huge amount of monetary stimulus, in turn, compensated for the lack of income generation in two ways. First, it encouraged a vast increase in household borrowing that directly supported consumer spending. While debt levels soared relative to incomes, the super-low interest rates have kept monthly debt-servicing burdens steady throughout the past three years. What's more, mortgage debt accounted for the lion's share of the stepped-up borrowing, partly because low rates made homeownership affordable to millions of lower-income families. For those homebuyers, mortgage payments simply replaced rental payments instead of adding to monthly expenses.

Second, the Fed's low-rate strategy fueled one of the strongest housing booms ever, generating a huge appreciation in real estate values. As a result, homeowners enjoyed a tremendous buildup in housing equity, which they extracted through mortgage refinancings and home sales. Indeed, the volume of equity extraction alone just about equaled the wages foregone due to the absence of job growth.

But with the Federal Reserve Open Market Committee now on a rate-hiking course, the housing sector is set to cool from the torrid pace of recent years. Most industry analysts expect home values to appreciate at a much slower rate in coming months, if at all. Meanwhile, mortgage refinancings have receded sharply from the peak volume of the Spring, thanks to higher mortgage rates, and households have already borrowed to the max against their homes. Federal Reserve data show that mortgage debt as a percent of owner-occupied properties has shot up by 3 percentage points over the past three years, moving further into record-high territory.

With the impetus from housing fading, and monetary and fiscal policies turning less accommodative, the need for stronger income growth to sustain consumption becomes more imperative. That's why the improving job market that got underway last summer and gained traction this year was such a welcome development. More than anything, it represented a transition away from an asset and wealth-dependent economy to one that is driven primarily by organic sources of

strength, namely job and income growth. Indeed, the Fed's decision to begin removing monetary stimulus from the system, by boosting interest rates .25 percent for the first time in four years, reflects its perception that the traditional internal dynamics of the business cycle is taking hold.

No doubt, that perception may now come under closer scrutiny in light of the late spring slowdown in hiring and consumer spending. Some Fed analysts already contend that future rate increases should be delayed until the economy regains its footing. However, unless upcoming data for July, especially the jobs report, are exceptionally weak, that's not likely to happen. While the economy may have hit a speed bump, it has not been derailed from the recovery track. What's more, any sign that the Fed is prolonging its exceptionally easy monetary policy beyond the point of need would only fuel an unwanted increase in inflation expectations.

More than likely, the recent slowdown reflects transitory forces, particularly the upward climb in oil prices this year that has sapped consumer purchasing power. According to some estimates, higher oil bills have siphoned about \$50 billion from household budgets which, like a tax increase, is bound to cut into discretionary spending. The energy outlook is always muddled by geopolitical events, and it is even more so now because of the volatile nature of the Mid-east situation. But the fundamentals suggest that oil prices should stabilize, if not decline, later this year owing to slowing demand from China and higher OPEC production.

Meanwhile, the June cutback in hiring should not obscure the fundamental improvement that is taking place in the labor market. For the second quarter as a whole, companies added 671 thousand workers to payrolls, compared to 595 thousand in the first quarter. While employment gains may not approach the 339 thousand monthly average of March and April, company surveys indicate that job formation should be strong over the second half of the year, providing the long-delayed income generation needed to support consumption.

Moreover, if oil prices stabilize, the most powerful catalyst behind the pickup in inflation this year will also subside. That won't preclude further upward price pressures, which normally occurs as the expansion matures and resource slack is gradually used up. But there is still a lot of catching-up to do before price pressures reach a boiling point, requiring tough anti-inflation measures by the Fed. Simply put, the cycle is entering a normal stage, which justifies a normalization of monetary policy. The pace at which the Fed moves interest rates up to a neutral level, which neither stimulates nor subtracts from growth, will be

heatedly debated as the economy waxes and wanes in coming months. But the crosscurrents buffeting the economy would seem to support the "measured" course of action Chairman Greenspan is intent on following. Finally, consumer confidence has been rising for the past four months as the economy has been on a path to recovery. The Associated Press Consumer Confidence Index climbed to 104.8 in August, up from 92.0 in July, led by consumers' perceptions of their own finances and optimism about how their local economy will be doing six months from now. The snapshot of consumer sentiment found Americans considerably more upbeat about the economy than a year ago, when the index was 89.0.

The most likely outcome, when considering all of the above as it relates to the national picture, is that the economy will regain momentum through the end of this year and into 2005. Moreover, despite recent events such as the continuing war on terrorism, our long-term prospects are bright. The U.S. economy has proven itself resilient and dynamic, driven by an entrepreneurial culture, market-based principles and continuing technological advances. These factors have enhanced the economy's ability to handle challenges and have laid the foundation for solid growth and price stability in the years ahead.

State Economy – Michigan's unemployment rate dropped slightly in June, 2004 to 6.5 percent, one-tenth of a percentage point lower than last month. The State's unemployment rate remains almost a full percentage point higher than the national average of 5.6 percent. Last June, the State's unemployment rate was 7.3 percent. Overall, more than 4.71 million people were employed in Michigan in the month of June, compared to a six-month average of 4.73 million.

Michigan is poised for a modest rebound in manufacturing jobs, offering new hope that a formula can be found for a prosperous economic future despite the domestic auto industry's long decline. The economic comeback well under way across the nation soon will spread to Michigan, according to a new study by the University of Michigan. As in the past, a stronger national economy will mean more work for Michigan factories.

The turnaround got started in April, spurred by declining interest rates, federal tax cuts and a healthy auto market, and will become stronger next year, the study predicts. Over the course of this year, Michigan will wipe out its first-quarter job losses and gain back 18,000 additional jobs. The study forecasts a gain of 84,000 jobs in 2005, with all sectors of the economy showing growth, including manufacturing. Driven by the introduction of a record number of new vehicle designs in 2006, auto sales are expected to reach a new peak by the end of the decade. Sales could exceed 18 million, up from the last record of 17.2 million in 2000.

Michigan, still the nerve center for the North American auto industry, should get a boost from that.

But the recovery will be short-lived unless the State takes action to mend several disturbing trends that have spread gloom across the State in the past two years. Michigan clearly is at a critical point, with the prosperity it has enjoyed ever since the end of World War II at risk.

The 30-year trend of declining factory employment accelerated during the last five years. Educated young people have been leaving the State. In many parts of Michigan, roads, bridges and sewers need repair. Detroit's Big Three automakers, who put the muscle in the State economy for nearly a century, are getting kicked around by tough foreign competitors.

Poverty and lack of health insurance coverage have worsened in Michigan and average household income is down. Michigan's poverty rate for 2002-03 is pegged at 10.8 percent, compared to 10.3 percent in 2001-02. The national average is 12.1 percent. The Census Bureau's definition of poverty varies by household size. For instance, the threshold for a family of four during the latest period was \$18,810, while for two people it was \$12,015. Median household incomes in Michigan averaged \$45,176 in 2002-03, down from \$45,335 in 2001-02 – a decline of less than one percent. The national median was \$43,527. Eleven percent of the state's residents were without health insurance in 2002-03, an increase from 10.4 percent during 2001-02, but lower than the 15.1 percent nationwide rate for the latest period. It was the third consecutive period in which the state's performance declined in all three categories, going back to 2000-01. The poverty rate then was 9.7 percent, the median household income was \$46,929 and 9.9 percent of the state's population had no health insurance.

But an impoverished Michigan isn't inevitable. The State's 1990s rebound – the richest period of job creation in its history – proved as much. Manufacturing rebounded from the 1991 recession and virtually every job sector grew, producing the first labor shortages in modern Michigan history.

During the 1990s, Michigan had a vibrant residential and commercial construction sector, strong gains in service jobs, a substantial tourist industry, small but significant job gains in non-automotive high-tech industries, and significant growth in two-income households. Perhaps, most importantly, the State had the benefit – as well as the disadvantage – of the emerging global economy. Traditional Big Three jobs were lost, but many were replaced by even better jobs in factories, offices and technical centers of foreign-based auto companies and major suppliers. Japanese automaker Nissan, as just one example, now has more than

1,000 engineers and other workers in Metro Detroit locations. Flint's auto plants withered, but Oakland County's Automation Alley – a collection of high-tech related businesses – boomed.

Rising worldwide competition and new, more efficient, manufacturing methods in the auto industry killed many of the State's high-paying, low-tech factory jobs. But Michigan remains – for the foreseeable future – the nation's No. 1 auto production state, rich with skilled employment. Consequently, there has been a renewed emphasis on retraining displaced workers for new jobs, as well as bolstering the technical acumen of those still at work in Michigan factories.

To secure its economic future, the State must retain a solid core of auto employment – which now seems likely – while investing wisely in education, job retraining, entrepreneurship and infrastructure. Governor Jennifer Granholm has made it a priority to boost the number of college graduates the State produces. At present, the percentage of Michiganders with bachelor's degrees falls a couple of percentage points below the national average of 24 percent, but at least two points behind specific states such as Massachusetts, Maryland and Colorado. Per-capita income for those specific states is as much as \$18,000 higher than that of Michigan. Progress in learning, while vital, won't be easy. The Governor has established a special commission to figure out how to produce more college graduates, especially in growth fields such as high-technology engineering and life sciences.

The State also is banking on new technology in biological sciences and security, as well as manufacturing, to create jobs. Forecasters project health care, pharmaceuticals and energy are industries that will continue to grow, even as manufacturing levels off. Michigan's life science industry alone currently has 540 companies and 32,000 workers, tenth largest in the U.S., according to the State's Economic Development Corporation (EDC). While that's a small portion of Michigan's 4.2 million jobs, the EDC has received 131 applications for State grant money to start up companies utilizing new technologies.

High-quality employment growth in Michigan can also come in service-oriented activities, such as entertainment and travel. Florida does fine with no auto industry. The U.S. Labor Department expects the service industry to add 428,000 jobs in Michigan over the next ten years, and they won't all be modest paying.

The debate goes on as to whether or not Michigan is a friendly place in which to do business. Some of the arguments put forth on Michigan's behalf are based on some of the following strengths:

- Business incentive packages, through the Michigan Economic Growth Authority, that are among the best anywhere;
- More engineers than most other states and one of the world's top engineering schools at the University of Michigan;
- No toll roads;
- Epicenter of North American auto manufacturing;
- More skilled trades than any other state;
- A very good university system and excellent community colleges;
- Basic infrastructure for industry, meaning lower average water, sewer and road-building costs to new businesses;
- Great Lakes, natural beauty and plentiful water.

Local Economy - Adrian community leaders have been on the cutting edge of attracting and promoting commerce throughout the City's history, from establishing the first railroad East of the Alleghenies in 1836 to obtaining one of the first Michigan Economic Growth Authority (MEGA) tax credits for the Solvay Automotive Project in 1995. The Adrian area serves as the corporate headquarters for several businesses including Merillat Industries (a division of Masco). The Gleaner Life Insurance Society, the Kapnick Insurance Company and others.

The employer base remains diversified with several less recession-sensitive employers located in the community including governmental (City and County governments and a State Police Post) educational (Adrian College, Siena Heights College, Adrian Public Schools and the Intermediate School District, as well as the ISD-Vocational Education Center) and institutional organizations (Bixby Medical Center and Michigan Correctional Facility).

During the past year, over \$14 million of new commercial and industrial assessed value was added to the City tax roll. Even though the City is nearly built-out within its current boundaries, the year-to-year value added comes from business expansion and related additions to the Personal Property tax roll as a result of the City Commission's continued efforts to implement pro-active community redevelopment and revitalization strategies. The Brownfield Redevelopment Authority has adopted several redevelopment plans, including an initiative that could result in up to \$65 million of new investment in Adrian by Delphi

Automotive. The City Commission has financially supported the Downtown Development Authority in the development of a comprehensive revitalization action plan for the downtown and the newly created position of Downtown Development Director is in the process of implementing the plan. To attract shoppers to downtown retailers, parking meters have been removed in favor of 2-hour free parking on streets and 3-hour free parking in City lots. The City's Streetscape is being expanded west on Maumee Street, and the study to convert one-way streets to two-way traffic circulation is underway.

The poor job's market currently plaguing the state and national economies is adversely impacting Lenawee County as well. Joblessness rose to 8.0 percent in July from 6.6 percent in June, which is an increase of 1,125 people out of work. Unemployment was 4,200 in July, compared to 3,175 in June, caused by summer plant layoffs and plants shutting down due to model changeover. The City of Adrian experienced an unemployment rate of 10.2 percent in July compared to 7.8 percent in June.

The Lenawee County Chamber of Commerce has contracted with the University of Michigan Business School to do an assessment of local business conditions with the intent of identifying constraints to economic growth and developing recommended measures for eliminating or minimizing those constraints. For example, certain specific manufacturing sectors which predominate the industrial component of Lenawee County are seeing significant production shifts from the United States to China, such as paper mills, chemicals, plastics, fabricated metals and industrial machinery. New investment in large industry assets with high capital requirements is very unlikely to become a reality, as there is little or no prospective growth due to overall excess capacity, and the Midwest does not have competitive operating costs. Recommended solutions include developing niche markets for proprietary products that cannot easily be turned into cheap commodities, which would entail significant investment in research & development. Also, government and private partnerships should initiate actions to reduce health care and workers compensation costs thereby improving businesses competitive position globally. Similarly, business regulations should be reduced and tax incentives increased.

Having a more diversified portfolio of economic activities and a broader range of job opportunities would not only protect the local workforce from national and global threats but also create high-wage challenging job opportunities beyond traditional sectors, helping to retain human capital in the region. Proposed solutions collected from interviews and focus groups are:

- Develop suppliers focused on serving small- and mid-sized companies in Jackson, Ann Arbor, Detroit and Toledo. Companies should concentrate on services, including design and engineering, or light manufacturing with customized simple tasks for which location is a competitive advantage.
- Take advantage of relative lower operating costs in Lenawee County compared to Washtenaw County.
- Leverage transfer of technology from local academic institutions. Strengthen collaboration between businesses and colleges, by having internship programs, career fairs and applied research programs.
- Develop agricultural related businesses, such as food processing, dairy processing, farmer's markets and specialty farming.
- Link a formal farmland preservation program with specialization in some crops, vegetables and livestock combined with added-value operations.
- Adopt rehabilitation codes and government sponsored loan programs to make developing old buildings easier.
- Leverage metal working competencies of region; population already trained in manufacturing jobs.
- Small companies play an important role in the City and County's economy today. Any strategy to define the local economic future needs to account for this major economic segment. In this regard the City Commission recently adopted a Local Preference Purchasing Policy in an attempt to stimulate local business retention and growth.

Finally, the analysis of survey results, more focused group discussion, and support from the comprehensive region profile of current economic conditions will determine the most suitable new business opportunities to reposition the local workforce, to determine a controlled growth in the region, to sustain local agriculture and to attract and retain a highly skilled youth population. A specific outcome of the completed project will be a plan with recommended activities, indicating responsible organizations and institutions, schedule and milestones, and projected funding requirements including potential sources of funding.

Long Term Financial Planning – Each December the City Commission and Department Heads convene to develop a five-year strategic plan for capital improvements. Highlights of the current program include:

- the continuing upgrade of computer technology throughout the City departments,
- prudent use of the \$18 million Fee Estate endowment to expand passive recreation throughout the community, such as the recent completion of the Trestle Park Boardwalk,
- the City Commission established a challenge grant to match private contributions to fund the construction of a skate park,
- Burr Ponds Park renovation is in the design phase, with the intention of making water resources accessible to park users,
- Requests for Proposal have been issued for a new Parks and Forestry Maintenance Facility,
- Street tree inventory was completed in 2002 and an additional 700 new planting sites will be added to the 6,500 trees currently existing on City right-of-ways,
- The burial records of the 19,000 former residents interred at the Oakwood Cemetery since 1848 have been computerized to aid visitors and researchers in their identification and location efforts,
- Additional facility upgrades are scheduled to Heritage Park which houses a baseball complex, soccer fields, disc golf facility, model airplane field, and picnic area, as well as a conference center,
- Voters recently approved a two-year fourteen (14%) percent telephone surcharge to support the Lenawee County Central Dispatch to update the 911 system by adding computer-aided dispatch (CAD) Countywide,
- replacement of the Police Department's record management software,
- Fire Department equipment has been upgraded and expanded to better serve homeland security requirements,
- the City Clerk plans to upgrade the City's election system and initiate a new electronic archiving system that will facilitate access to City records and save space,
- infrastructure improvements are progressing throughout the City, including implementation of a storm-water separation project, accelerated sidewalk repair and replacement program and many street improvement projects, as well as installation of an electric generator to eliminate power interruptions that cause sanitary sewer overflows and plant permit violations,

- the Utilities Department has identified a new ground water source that has the capability of replacing the current surface water source of the City's potable water supply,
- refurbish City Hall,
- continued additions to the book collection of the Adrian City Library's \$25 million inventory.

Long-range financial planning, of course, is affected by the City's revenue stream. The negative effects of "Proposal A" of 1994 are finally coming home to roost, particularly for older, low-growth rate communities like Adrian. The full impacts of this proposal on local government service levels were delayed by the unusually long robust economy experienced through the mid- and late 1990s. Proposal A will reduce City General Fund revenues from property taxes by about \$750,000 during fiscal year 2003-04 alone. Because of the State's greater reliance on the sales tax as a revenue producer, the slowing economy had a greater relative effect on State shared revenue payments, on which about 1/3 of the City's General Fund revenues are dependent. On the other hand, auguring in the City's favor is the fact that State shared revenue formulas are also highly population-weighted. Therefore on the brighter side, the Federal Census Bureau has corrected the City of Adrian's census count, adding 641 persons. This has resulted in the City actually gaining 118 people between 1990 and 2000, instead of the 523-person loss that the original faulty count indicated. This extra population may result in the City realizing up to \$80,000 per year more in State shared revenues than originally contemplated. It should be noted that the policy of the State Department of Treasury regarding the use of population figures in the calculation of State Revenue Sharing payments is adjusted in those communities that have State correctional facilities. The population figure before and after the aforementioned census correction has been reduced by one-half of the 294 occupants of the State juvenile correctional facility located in the City of Adrian.

Fund Balance – General Fund

Governmental Funds report the difference between assets and liabilities as *fund balance*, which is divided into *reserved* and *unreserved* portions. The function of *reserved fund balance* is simply to isolate the portion of fund balance that is *not* available for the following period's budget, so that *unreserved fund balance* can serve as a measure of currently available financial resources.

The reservation of fund balance is necessary for two reasons:

- *Resources not available for spending.* Some of the assets reported in governmental funds are not available for spending in the subsequent year's budget. For example, a *long-term* loan receivable, such as an advance to another fund, is not available for *current* spending. Likewise, governments like the City of Adrian that elect to report supplies, inventories and prepaid items in governmental funds typically would report a corresponding amount of *reserved fund balance* to indicate that these amounts are not actually available for spending.
- *Legal restrictions on spending.* Fund balance is also reserved to indicate situations where a portion of fund balance is not available for new spending because of legal restrictions involving parties outside the financial reporting entity. The most common example is amounts reserved for encumbrances, which represent contracts for goods or services with outside parties that are still outstanding at the end of the period and that the City intends to honor.

Unreserved fund balance may, in turn, be subdivided into *designated* and *undesignated* portions. Designations represent management's intended use of resources and should reflect actual plans approved by the City's senior management. Expressed another way, designations reflect a government's self-imposed limitations on the use of otherwise available current financial resources.

The following schedule presents an analysis of changes in General Fund – Fund Balance between FY2002-03 and FY2003-04:

**CITY OF ADRIAN
GENERAL FUND - FUND BALANCE**

General Fund – Fund Balance as of June 30, 2003	\$7,468,554
Reserves for:	
Inventories and Prepayments	155,888
Encumbrances	<u>1,724,487</u>
Total Reserved Fund Balance as of June 30, 2003	1,880,375
General Fund-Unreserved Fund Balance as of June 30, 2003	\$5,588,179
 FY2003-04 Revenue and Other Sources	 \$10,874,850
FY2003-04 Expenditures	<u>11,106,311</u>
Revenue Over/(Under) Expenditures	(\$231,461)
(Increase)/Decrease in Inventories and Prepayments	<u>(3,153)</u>
(Increase)/Decrease in Encumbrance Reservation	<u>956,035</u>
General Fund-Unreserved Fund Balance as of June 30, 2004	\$6,309,606

Inventories and Prepayments	\$159,041
FY2003-04 Encumbrances & Appropriations Carry-forward	768,452
Total Reserved Fund Balance as of June 30, 2004	<u>927,493</u>

General Fund – Fund Balance as of June 30, 2004	\$7,237,093
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Increase/(Decrease) in Fund Balance	<u>(\$231,461)</u>
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General Fund Unreserved Fund Balance as of June 30, 2004	<u>\$6,309,600</u>
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Proposed Designations of General Fund-Unreserved Fund Balance (Acct. #393.000):

1 DPW-Motor Pool - Depreciation Catch-Up	\$1,100,000	
2 City Hall Renovations	950,000	
3 Funding for FY2004-05 Budget	576,518	
4 Parks & Forestry Building	400,000	
5 Technology Infrastructure Upgrades	400,000	
6 Property Acquisitions and Options (Pearl Street, Other)	350,000	
7 Geographic Information System	225,000	
8 Increase in Actuarially Determined Pension Contribution	132,000	
9 Financial System (Including Utility Billing System)	125,000	
10 Street Sweeper	125,000	
11 Technology Training	50,000	
12 Information Technology - Depreciation Catch-Up	31,750	
13 City Clerk/Police Department - Document Imaging System	26,000	
14 Local Grant Match	25,000	
Total Proposed Designations		\$4,516,268

Undesignated Fund Balance	<u>\$1,793,332</u>
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Cash Management Policies and Practices – Cash temporarily idle during the year was invested in demand deposits, certificates of deposit, and obligations of the U.S. Treasury, as well as Investment Grade Commercial Paper (Rated A2/P2 or higher by Standard & Poor's and Moody's Investor Services, respectively). The exhibit below shows the amount of interest earnings by each type of fund during the 2003-04 fiscal year.

<u>Fund Type</u>	<u>Interest Income</u>
General Fund	\$119,231
Other Governmental Funds	51,648
Proprietary Funds	108,408
	<u>\$279,287</u>

City of Adrian investment policy specifies that all public funds held by the City, including federal funds, shall be deposited and/or invested with agencies that are recognized and authorized by Michigan statutes for that purpose. All certificates of investments of funds entrusted to the City of Adrian shall remain in the custody of the Finance Department unless otherwise authorized by the City Commission. As of June 30, 2004, all certificates of investments were in custody of the Finance Department.

Risk Management – The City is a member of the Michigan Municipal Liability and Property Pool for its general liability coverage and a member of the Michigan Municipal Workers Compensation Fund for its workers' compensation coverage. Both pools are under the Michigan Municipal Program sponsored and administered by the Michigan Municipal League (MML).

The City pays annual premiums to the insurance pools. The pools are self-sustaining through member premiums, and each carries reinsurance through commercial companies for claims in excess of a minimum of \$1,000,000 for each specific occurrence, and to a minimum of \$2,000,000 in aggregate in excess of the pool loss reserve fund. Based on an historical claims analysis by the Finance Department, deductibles for Comprehensive General Liability, Personal Injury Liability and Public Officials Liability coverages have been increased from \$1,000 to \$5,000, resulting in an annual savings of almost \$30,000.

The City of Adrian has been selected as a BETA SITE by the MML for testing improved risk management assessment and reporting, scheduled for implementation in 2005.

Pension and Other Post-employment Benefits- The City of Adrian is a member of the Municipal Employees' Retirement System (MERS) of Michigan. The pension program is administered by the MERS Board under the provisions of the Municipal Employees' Retirement Act of 1984, as amended by Public Act 220 of 1996, as embodied in the MERS Plan Document. The pension program is categorized as a Defined Benefit Program with eligibility earned at age 60 with 8 or more years of credited service with annual retirement benefits for General Non-represented employees based on 2.0 percent of Final Average Compensation (FAC

defined as the three consecutive year period of credited service in which the average compensation paid is highest) times years of credited service. Employee contributions for General employees amount to 3.0 percent of salary while employer contributions equate to 5.0 percent. Upon recommendation of the City Administrator, the City Commission recently improved the Defined Benefit Program by reducing the required years of credited service to achieve full vesting rights from 10 year to 8 years. Pension benefits, as well as employee and employer contributions, for Represented employees are determined in the collective bargaining process. Total Regular Employee Contribution calculated by the actuary for Fiscal Year 2004-05 amounts to \$423,912. As of December 31, 2003, the Pension Plan had Net Assets of \$34,241,034 with an Unfunded Actuarial Accrued Liability of \$2,759,994.

Fiduciary Operation- The City of Adrian has a perpetual care fund from which the interest earnings are used to maintain the cemetery. Interest earnings amounted to \$25,901 for Fiscal Year 2003 and the investment balance is \$751,874 principal is \$52,533 more than last year.

Awards and Acknowledgements

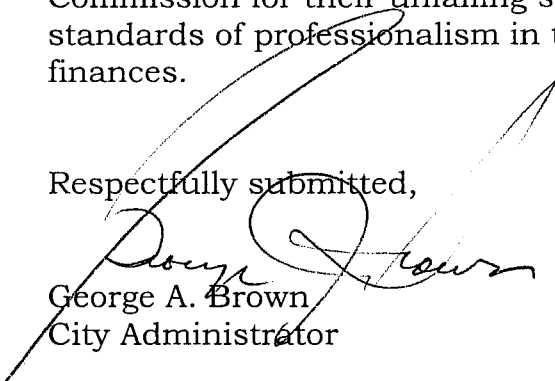
The Government Finance Officers Association (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the City of Adrian for its Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2003. The Certificate of Achievement is the highest form of recognition for excellence in state and local government financial reporting. This was the seventeenth consecutive year that the City has received this prestigious award.

In order to attain the Award, a government unit must publish an easily readable and efficiently organized Comprehensive Annual Financial Report with contents in conformance with program standards. Such Report must satisfy both generally accepted accounting principles (GAAP) and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement program requirements, and we are submitting it to GFOA for review.

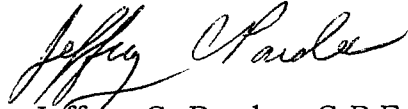
The preparation of the Comprehensive Annual Financial Report on a timely basis was made possible by the dedicated service of the entire staff of the Finance Department. Each member of the department has our sincere appreciation for the contributions made in preparation of this report.

In closing, credit must also be given to the Mayor and the City Commission for their unfailing support for maintaining the highest standards of professionalism in the management of the City of Adrian's finances.

Respectfully submitted,



George A. Brown
City Administrator



Jeffrey C. Pardee, C.P.F.O.
Finance Director

Certificate of Achievement for Excellence in Financial Reporting

Presented to

City of Adrian,
Michigan

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2003

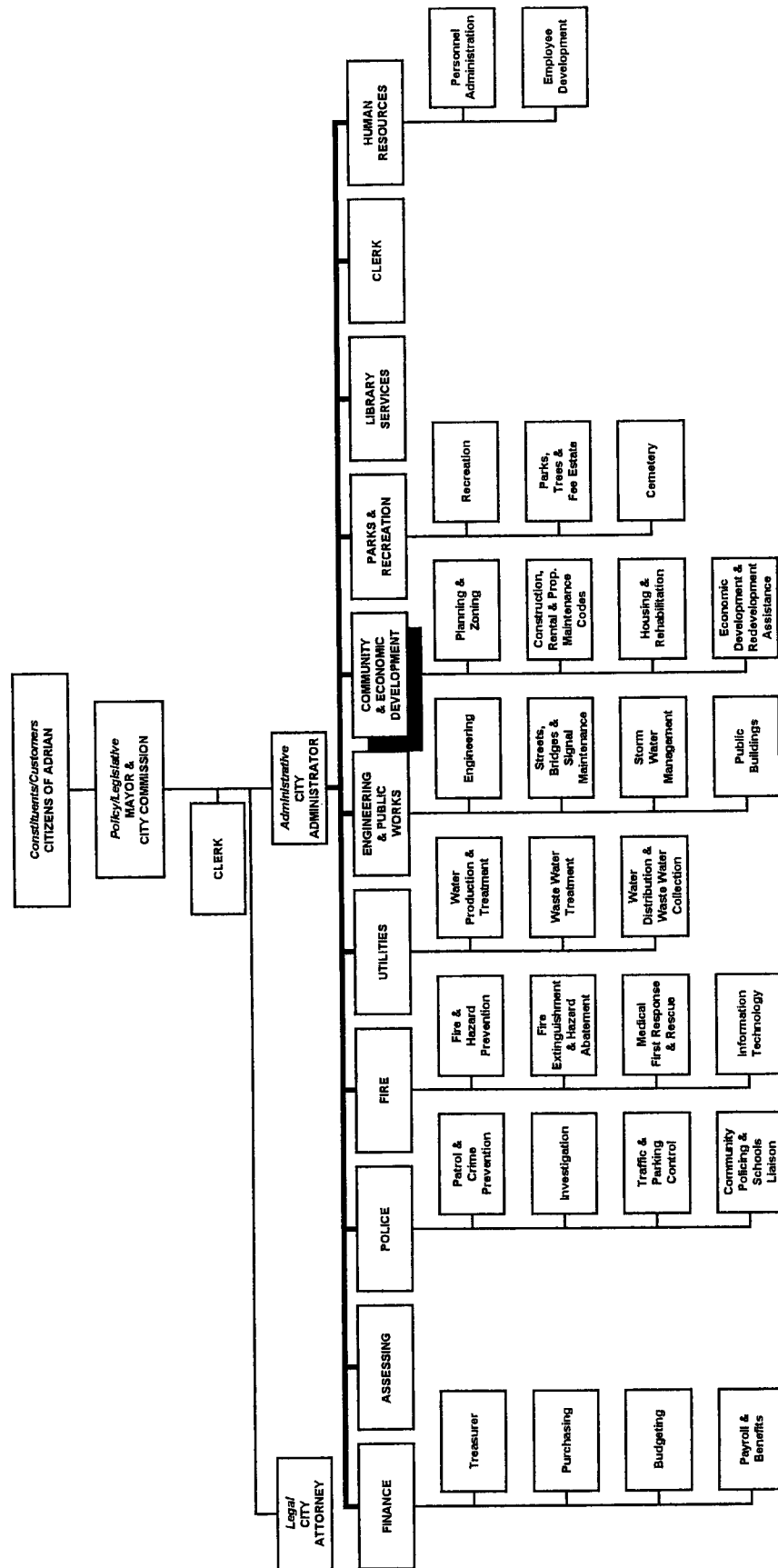
A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director

CITY OF ADRIAN ORGANIZATIONAL CHART



CITY OF ADRIAN, MICHIGAN
LIST OF PRINCIPAL OFFICIALS

JUNE 30, 2004

<u>NAME</u>	<u>TITLE</u>
Samuel Rye	Mayor
Charles E. Chase	Commissioner
Michael Clegg	Commissioner
Rhea Mills	Commissioner
Barb Mitzel	Commissioner
Gary McDowell	Commissioner
Eric Sullivan	Commissioner
George A. Brown	City Administrator
Jeffrey C. Pardee	Director of Finance
Maria Irish	Assessor
Michael S. Martin	Chief of Police
Paul G. Trinka	Fire Chief
Mark Gasche	Community Services Director
Jule J. Fosbender	Library Director
Keith Dersham	City Engineer
Marsha K. Rowley	City Clerk
James Caldwell	Director of Utilities
Jack Lewis	Personnel Director
Carol Konieczki	Community Development Director/Inspection

August 6, 2004

INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and
Members of the City Commission
City of Adrian, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Adrian, Michigan, as of and for the year ended June 30, 2004, which collectively comprise the City's basic financial statements as listed in the table of contents. We have also audited the aggregate nonmajor governmental funds, the aggregate nonmajor enterprise funds, and fiduciary fund type of the City of Adrian, Michigan, as of and for the year ended June 30, 2004, as displayed in the City's basic financial statements. These financial statements are the responsibility of the City of Adrian, Michigan's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the discretely presented component units, each major fund, and the aggregate remaining fund information as well as the aggregate nonmajor governmental funds, the aggregate nonmajor enterprise funds, and fiduciary fund type of the City of Adrian, Michigan, as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

August 6, 2004

To the Honorable Mayor and
Members of the City Commission
City of Adrian, Michigan

The management's discussion and analysis and pension plan schedule on pages 25 through 33 and page 77, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 6, 2004 on our consideration of the City of Adrian, Michigan's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Adrian, Michigan's basic financial statements. The introductory section, combining and individual nonmajor fund financial statements, and statistical tables are presented for purposes of additional analysis and are not a required part of the basic financial statements. The combining and individual nonmajor fund financial statements have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory section and statistical tables have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements of the City of Adrian, Michigan. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Robertson, Eaton & Owen, P.C.

August 6, 2004

**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL
REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and
Members of the City Commission
City of Adrian, Michigan

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Adrian, Michigan, as of and for the year ended June 30, 2004, which collectively comprise the City of Adrian, Michigan's basic financial statements and have issued our report thereon dated August 6, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

COMPLIANCE

As part of obtaining reasonable assurance about whether the City of Adrian, Michigan's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit, we considered the City of Adrian, Michigan's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no

Page 2

August 6, 2004

To the Honorable Mayor and
Members of the City Commission
City of Adrian, Michigan

matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to management of the City of Adrian, Michigan in a separate letter dated August 6, 2004.

This report is intended solely for the information and use of management, the City Commission, Departments of the State of Michigan, and federal awarding agencies and pass through entities and is not intended to be and should not be used by anyone other than these specified parties.

Robertson, Eaton & Owen, P.C.

August 6, 2004

**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO
MAJOR PROGRAMS AND ON INTERNAL CONTROL OVER COMPLIANCE
IN ACCORDANCE WITH OMB CIRCULAR A-133**

INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and
Members of the City Commission
City of Adrian, Michigan

COMPLIANCE

We have audited the compliance of the City of Adrian, Michigan with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 *Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2004. The City of Adrian, Michigan's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal programs is the responsibility of the City of Adrian, Michigan's management. Our responsibility is to express an opinion on the City of Adrian, Michigan's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City of Adrian, Michigan's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City of Adrian, Michigan's compliance with those requirements.

In our opinion, the City of Adrian, Michigan complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2004.

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August 6, 2004

To the Honorable Mayor and
Members of the City Commission
City of Adrian, Michigan

INTERNAL CONTROL OVER COMPLIANCE

The management of the City of Adrian, Michigan is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City of Adrian, Michigan's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal programs being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of management, the City Commission, Departments of the State of Michigan, and federal awarding agencies and pass through entities and is not intended to be and should not be used by anyone other than these specified parties.

Robertson, Eaton & Owen, P.C.

CITY OF ADRIAN, MICHIGAN
COMPREHENSIVE ANNUAL FINANCIAL STATEMENT
Management's Discussion and Analysis
October 18, 2004

As management of the City of Adrian, we offer readers of the City of Adrian's financial statements this narrative overview and analysis of the financial activities of the City of Adrian for the fiscal year ended June 30, 2004. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal, which can be found on pages 1-22 of this report. All amounts, unless otherwise indicated, are presented in whole dollars

Financial Highlights

- The Assets of the City of Adrian exceeded its liabilities at the close of the most recent fiscal year by \$68,324,700 (*net assets*). Of this amount, 11,750,826 (*unrestricted net assets*) may be used to meet the government's ongoing obligations to citizens and creditors.
- The City's total net assets decreased by (\$130,754). The decrease is primarily attributable to the \$415,599 operating shortfall in Governmental Activities (\$231,461 in the General Fund), offset by the favorable \$284,845 operating variance for Business-Type Activities.
- As of the close of the current fiscal year, the City of Adrian's governmental funds reported combined ending fund balances of \$11,984,923, a decrease of \$195,032 in comparison with the prior year. Although revenue decreased by \$1.1 million (Federal and State revenue down \$883,110; Interest earnings down \$116,239), expenditures decreased a like amount, primarily capital expenditures for Community Development and Parks & Recreation. Therefore the net decrease is mainly attributable to General Fund operating subsidies to the Dial-A-Ride (\$121,552 and the Automobile Parking System (\$47,575). Approximately three-fourths of the total fund balance, \$9,049,035, is *available for spending* at the City Commission's discretion (*unreserved fund balance*).
- At the end of the current fiscal year, unreserved fund balance for the general fund was \$6,309,600 or fifty-six (56%) percent of total general fund expenditures. Of this amount, management has designated \$4,516,268 for the following specific projects, leaving \$1,793,332 in Unreserved/Undesignated Fund Balance.

1)	DPW-Motor Pool – Depreciation Catch-UP	\$1,100,000
2)	City Hall Renovations	950,000
3)	Funding for FY2004-05 Budget	576,518
4)	Parks & Forestry Building	400,000
5)	Technology Infrastructure Upgrades	400,000
6)	Property Acquisitions and Options	350,000
7)	Geographic Information System	225,000
8)	Increase in Actuarially Determined Pension Contr.	132,000
9)	Financial System (Including Utility Billing System)	125,000

10)	Street Sweeper	125,000
11)	Technology Training	50,000
12)	Information Technology – Depreciation Catch-Up	31,750
13)	City Clerk/Police Department – Document Imaging	26,000
14)	Local Grant Match	25,000
	Total	<u>\$4,516,268</u>

- The City of Adrian’s total debt burden increased by \$6,207,860 or fifty-nine (59%) percent during the current fiscal year. The key factors in this increase were the issuance of revenue bonds through the Michigan Revolving Loan Fund for Wastewater System Improvements (authorized up to \$9,000,000 with a loan balance of \$8,920,000 as of 6/30/2004) and Water Supply System improvements (authorized up to \$8,000,000 with a loan balance of \$5,665,000 as of 6/30/2004). Decreased debt obligations were realized due to retirement of remaining balance of 1991 Water System Revenue Bonds (\$250,000), payment against Automobile Parking Bonds (\$50,000, leaving a balance of \$50,000), Storm Water Utility Bonds (\$90,000, leaving a balance of \$295,000), and Parks & Recreation Installment Purchase Contracts (\$189,583, leaving a balance of \$1,810,808).

Overview of the Financial Statements

This discussion and analysis are intended to serve as an introduction to the City of Adrian’s basic financial statements. The City of Adrian’s basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-wide Financial Statements. The *government-wide financial statements* are designed to provide readers with a broad overview of the City of Adrian’s finances, in a manner similar to private-sector business.

The *Statement of Net Assets* presents information on all of the City of Adrian’s assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City of Adrian is improving or deteriorating.

The *Statement of Activities* presents information showing how the City’s net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the City of Adrian that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The governmental activities of the City of

Adrian include general government, public safety, highways and streets, sanitation, economic development, and culture and recreation. The business-type activities of the City of Adrian include water and sewer operations and automobile parking activities.

The government-wide financial statements include not only the City of Adrian itself (known as the *primary government*), but also a legally separate Downtown Development Authority and a legally separate Local Development Finance Authority for which the City of Adrian is financially accountable. Financial information for these *component units* is reported separately from the financial information presented for the primary government itself. The Dial-A-Ride transportation system and OMNI drug enforcement unit function for all practical purposes as departments of the City of Adrian and, therefore, have been included as an integral part of the primary government. The government-wide financial statements can be found on pages 34-36 of this report.

Fund Financial Statements. A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City of Adrian, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City of Adrian can be divided into three categories: governmental funds, proprietary funds and fiduciary funds.

Governmental Funds. Governmental funds are used to account for essentially the same functions reported as *governmental activities* in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The City of Adrian maintains ten individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures and changes in fund balances for the general fund, major streets and local street funds, and the Fee and Public-Purpose Fund, all four of which are considered to be major funds. Data from the other six governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of *combining statements* elsewhere in this report.

The City of Adrian adopts an annual appropriated budget for its general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget. The basic governmental fund statements can be found on pages 37-39 of this report.

Proprietary Funds. There are traditionally two different types of proprietary funds. *Enterprise funds* are used to report the same functions presented as *business-type activities* in the government-wide financial statements. The City of Adrian uses enterprise funds to account for its water and sewer operations and for the Automobile Parking and Dial-A-Ride Systems, as well as the Capital Projects Revolving Fund and Storm Water Utility Fund. *Internal service funds* are an accounting device normally used to accumulate and allocate costs internally among the City of Adrian's various functions. The City of Adrian does not presently use this fund category, however, an Information Technology Fund will be established with the implementation of the FY2004-05 Budget.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the Water System and the Wastewater System, both of which are considered to be major funds of the City of Adrian. Conversely, the Capital Projects Revolving Fund, Dial-A-Ride, Storm Water Utility and the Automobile Parking System funds are combined into a single, aggregated presentation in the proprietary fund financial statements. Individual fund data for these enterprise funds is provided in the form of *combining statements* elsewhere in this report. The basic proprietary fund financial statements can be found on pages 46-50 of this report.

Fiduciary Funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are *not* available to support the City of Adrian's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds.

The basic fiduciary fund financial statements can be found on page 51 of this report.

Notes to the Financial Statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 52-77 of this report.

Other Information. In addition to the basic financial statements and accompanying notes, this report also presents certain *required supplementary information* concerning the City of Adrian's progress in funding its obligation to provide pension benefits to its employees through employer contributions and required employee contributions. Required supplementary information can be found on page 77 of this report.

The combining statements referred to earlier in connection with non-major governmental funds and enterprise funds are presented immediately following the required supplementary information on pensions. Combining and individual fund statements and schedules can be found on pages 78-126 of this report.

Economic Condition Reporting: The Statistical Section

The Governmental Accounting Standards Board (GASB) has issued Statement 44 regarding Economic Condition Reporting for General Purpose Local Governments. Although the provisions of Statement 44 are effective for Statistical Sections prepared for periods beginning after June 15, 2005, the City of Adrian seeks to meet the intent of this Statement through early adoption and by improving the understandability and usefulness of the Statistical Section information by addressing traditional comparability issues that have developed in practice and by adding information from the new financial reporting model for state and local governments required by Statement 34.

Statement 44 establishes the objectives of the Statistical Section and the five categories of information it contains – financial trends information, revenue capacity information, debt capacity information, demographic and economic information, and operating information.

This part of the City of Adrian's comprehensive annual financial report presents detailed information as a context for understanding what the information in the financial statements, note disclosures, and required supplementary information says about the City's overall financial health.

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These schedules contain trend information to help the reader understand how the City's financial performance and well-being have changed over time.

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Government-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the City of Adrian, assets exceeded liabilities by \$68,324,700 at the close of the most recent fiscal year.

By far the largest portion of the City of Adrian's net assets (75 percent) reflects its investment in capital assets (i.e., land, buildings, machinery and equipment), less any related debt used to acquire those assets that is still outstanding. The City of Adrian uses these capital assets to provide services to citizens; consequently, these assets are *not* available for future spending. Although the City of Adrian's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to pay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

CITY OF ADRIAN'S NET ASSETS

FY
2004

	Governmental Activities	Business- Type Activities	FY2004	FY2003
Current and Other Assets	\$12,318,579	\$6,943,938	\$19,262,517	\$22,602,103
Capital Assets	25,572,059	41,272,525	66,844,584	59,495,801
Total Assets	<u>\$37,890,638</u>	<u>\$48,216,463</u>	<u>\$86,107,101</u>	<u>\$82,097,904</u>
Long-Term Liabilities Outstanding	\$404,829	\$216,630	\$621,459	\$10,422,798
Other Liabilities	2,120,351	15,040,591	17,160,942	3,219,652
Total Liabilities	<u>\$2,525,180</u>	<u>\$15,257,221</u>	<u>\$17,782,401</u>	<u>\$13,642,450</u>
Net Assets:				
Invested in Capital Assets, net of Related Debt	\$23,761,251	\$26,559,550	\$50,320,801	\$51,698,113
Restricted	4,747,830	1,505,243	6,253,073	6,006,406
Unrestricted	6,856,377	4,894,449	11,750,826	10,750,935
Total Net Assets	<u>\$35,365,458</u>	<u>\$32,959,242</u>	<u>\$68,324,700</u>	<u>\$68,455,454</u>

An additional portion of the City of Adrian's net assets, seventeen (9.1%) percent, represents resources that are subject to external restrictions on how they may be used. The remaining balance of *unrestricted net assets* (\$11,750,826) may be used to meet the City's ongoing obligations to citizens and creditors.

As indicated earlier, the City's total net assets decreased by (\$130,754). The decrease is primarily attributable to the \$415,599 operating shortfall in Governmental Activities (\$231,461 in the General Fund), offset by the favorable \$284,845 operating variance for Business-Type Activities. The City of Adrian, however, is able to report positive balances in the remaining categories of net assets (Restricted and Unrestricted), both for the government as a whole, as well as for its separate governmental and business-type activities.

Governmental Activities. A summary of Governmental Activities follows:

CITY OF ADRIAN STATEMENT OF ACTIVITIES FY2004				
	Governmental	Business-		
	Activities	Type		
		Activities	FY2004	FY2003
Expenses (Over)/Under Revenues				
Functions/Programs:				
General Government	(\$1,288,721)		(\$1,288,721)	(\$1,629,766)
Public Safety	(4,248,675)		(4,248,675)	(3,763,299)
Public Works	(1,074,209)		(1,074,209)	(918,339)
Culture & Recreation	(760,884)		(760,884)	(1,235,699)
Other Services	(1,091,531)		(1,091,531)	(392,928)
Community/Economic Development	(26,930)		(26,930)	108,505
Highways, Streets & Bridges	(1,800,935)		(1,800,935)	(1,605,519)
Interest on Long-Term Debt	(78,673)		(78,673)	(87,538)
Wastewater System		(260,786)	(260,786)	(329,521)
Water System		347,740	347,740	190,638
Dial-A-Ride System		(121,919)	(121,919)	(46,865)
Automobile Parking System		(1,154)	(1,154)	(2,991)
Storm Water Utility		56,114	56,114	87,578
Total Activities	(\$10,370,558)	\$19,995	(\$10,350,563)	(\$9,625,744)
General Revenues:				
Property Taxes			\$6,041,046	\$5,914,288
Sales Tax			2,551,255	2,621,990
Motor Vehicle Fuel Tax			1,337,898	1,227,987
Grants and Contributions			11,008	660,115
Unrestricted Investment Earnings			266,602	367,063
Transfers			12,000	
Total General Revenues			\$10,219,809	\$10,791,443
Change in Net Assets			(\$130,754)	\$1,165,699
Net Assets - Beginning of the Year			\$68,455,454	\$67,289,755
Net Assets - End of the Year			\$68,324,700	\$68,455,454

Financial Analysis of the Government's Funds

As noted earlier, the City of Adrian uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds. The focus of the City's *governmental funds* is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the City of Adrian's financing requirements. In particular, *unreserved fund balance* may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year. As of the end of the current fiscal year, the City of Adrian's governmental funds reported combined ending fund balances of \$11,984,923, a decrease of \$195,032 in comparison with the prior year. Although revenue decreased by \$1.1 million (Federal and State revenue down \$883,110; Interest earnings down \$116,239), expenditures decreased a like amount, primarily capital expenditures for Community Development and Parks & Recreation. Therefore the net decrease is mainly attributable to General Fund operating subsidies to the Dial-A-Ride (\$121,552) and the Automobile Parking System (\$47,575). Approximately three-fourths of the total fund balance, \$9,049,035, is *available for spending* at the City Commission's discretion (*unreserved fund balance*). The remainder of the fund balance is *reserved* to indicate that it is not available for new spending because it has already been committed 1) to liquidate contracts and purchase orders of the prior period (\$1,561,978), 2) for loans receivable 3 (\$256,888), 3) to generate income to pay for the perpetual care of the municipal cemetery (\$751,584), or 4) for a variety of other restricted purposes (\$365,438).

The General Fund is the chief operating fund of the City of Adrian. At the end of the current fiscal year, unreserved fund balance of the General Fund was \$6,309,600, while total fund balance reached \$7,237,093. As a measure of the General Fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents fifty-six (56%) percent of the total General Fund expenditures, while total fund balance represents sixty-five (61%) percent of that same amount.

The fund balance of the City of Adrian's General Fund decreased by (\$231,461) during the current fiscal year. The key factor in this decrease is the General Fund operating subsidies to the Dial-A-Ride (\$121,552) and the Automobile Parking System (\$47,575), as well as a reduction in State Revenue Sharing (\$70,703).

Other Governmental Funds include Major Streets, Local Streets, and Fee & Public Purpose Funds, as well as other minor funds, such as Perpetual Care and Endowment Funds. Collectively, their fund balances increased by \$36,429, to \$4,747,830.

Proprietary Funds. The City of Adrian's Proprietary Funds provide the same type of information found in the government-wide financial statements, but in more detail.

Unrestricted net assets of the Water Fund at the end of the year amounted to \$1,396,400, an increase of \$664,613 attributable to a favorable variance in operations (\$372,085), a decrease in Capital Assets, net of related debt (\$253,514), and Interest Earnings (\$55,203).

Unrestricted net assets of the Wastewater Fund at the end of the year amounted to \$2,879,205, an increase of \$449,041 attributable to a decrease in Capital Assets, net of related debt (\$905,927), offset by an unfavorable variance in operations (\$248,050), and an increase in restricted amounts for debt service (\$208,836). The total growth in all Proprietary Funds was \$284,845, including Storm-Water Utility, Automobile Parking System, Dial-A-Ride System and Capital Projects Revolving Fund. Other factors concerning the finances of these funds have already been addressed in the discussion of the City of Adrian's business-type activities.

General Fund Budgetary Highlights

Differences in the original budget and the final amended budget amounted to \$1,215,967 increase in appropriations and can be briefly summarized as follows:

- \$124,684 appropriation for Dial-A-Ride subsidy;
- \$ 95,363 appropriations for Geographic Information System related activities;
- \$ 60,000 appropriation for Residential, Commercial & Industrial Reappraisal Project;
- \$ 58,367 appropriation for Parks- Capital Outlay, including Skate Park;
- \$ 53,000 appropriation for Organizational Assessment Project;
- \$ 53,000 appropriation for City Hall Workstations;
- \$ 49,866 appropriation for Loss on sale of 461 S. Main St. Property;
- \$ 47,575 appropriation for Auto Parking Fund subsidy;
- \$ 24,250 appropriation for Master Plan consultant; and
- \$649,862 appropriation for Mid-Year Budget Adjustments.

The above listed appropriations were budgeted from available fund balance. During the year, however, revenues exceeded budgetary estimates and expenses were less than budgetary estimates, thus eliminating the need to draw upon existing fund balance.

Capital Asset and Debt Administration

Capital Assets. The City of Adrian's investment in capital assets for its governmental and business-type activities as of June 30, 2004, amounts to \$66,844,584 (net of accumulated depreciation), representing a year-to-year increase of \$7,348,783, primarily attributable to Work-in-Progress related to Sewer and Water System improvements.. This investment in capital assets includes land, buildings and improvements, machinery and equipment, and park facilities, as well as roads, highways and bridges, and water/wastewater infrastructure. The total increase in the City of Adrian's investment in capital assets for the current fiscal year was 12.4 percent (a 1.8 percent decrease for governmental activities and a 23.4 percent increase for business-type activities).

CITY OF ADRIAN'S CAPITAL ASSETS
(net of depreciation)

	Governmental Activities		Business-Type Activities		Total	
	2004	2003	2004	2003	2004	2003
Land	\$7,510,774	\$7,300,656	\$904,592	\$911,062	\$8,415,366	\$8,211,718
Land Improvements	5,590,458	5,434,062	1,266,207	1,275,263	6,856,665	6,709,325
Buildings and Systems	2,053,529	2,125,053	0	0	2,053,529	2,125,053
Utility Systems	0	0	22,664,551	22,665,173	22,664,551	22,665,173
Machinery & Equipment	4,949,753	5,604,203	254,195	255,920	5,203,948	5,860,123
Infrastructure	5,467,545	5,443,658	0	0	5,467,545	5,443,658
Construction -In-Progress	0	143,600	16,182,980	8,337,151	16,182,980	8,480,751
Total Capital Assets	\$25,572,059	\$26,051,232	\$41,272,525	\$33,444,569	\$66,844,584	\$59,495,801

Long-Term Liabilities. At the end of the current fiscal year, the City of Adrian had total long-term liabilities of \$17,160,942. Of this amount, \$345,000 comprises debt backed by the full faith and credit of the City and \$14,585,000 of the debt represents bonds secured solely by specified revenue sources (i.e., revenue bonds). Other long-term liabilities include installment purchases through the Bank of Lenawee of \$1,810,808 for purchases of park property in Adrian and Madison Townships, as well as Accrued Sick and Vacation Compensation of \$420,134.

CITY OF ADRIAN'S LONG-TERM LIABILITIES
General Obligation and Revenue Bonds
Installment Purchase Obligations
Accrued Sick and Vacation

	Governmental Activities		Business-Type Activities		Total	
	2004	2003	2004	2003	2004	2003
General Obligation Bonds	\$0	\$0	\$345,000	\$485,000	\$345,000	\$485,000
Revenue Bonds	0	0	14,585,000	8,047,557	14,585,000	8,047,557
Installment Purchase	1,810,808	2,000,391	0	0	1,810,808	2,000,391
Accrued Sick & Vacation	309,543	367,701	110,591	147,474	420,134	515,175
Total Long-Term Liabilities	\$2,120,351	\$2,368,092	\$15,040,591	\$8,680,031	\$17,160,942	\$11,048,123

The City of Adrian's long-term liabilities increased by \$6,112,819 during the current fiscal year. The key factor in this increase was the issuance of revenue bonds through the State of Michigan to fund Water and Wastewater Infrastructure improvements..

On June 30, 2004, the City of Adrian had a number of debt issues outstanding. These issues consisted of general obligation bonds and revenue bonds. The City has maintained an A1 bond rating from Moody's Investor Services and an A rating from Standard & Poor's on general obligation issues. Under current State statutes, the City's general obligation outstanding debt amount is subject to a legal limitation based on 10 percent of total assessed value of real and personal property. As of June 30, 2004 the City's net general obligation bond and installment

debt of \$2,155,808 was well below the legal limit of \$38,356,011 and debt per capita equaled \$97.04. During the year, the City issued no new General Obligation bonds.

Additional information on the City of Adrian's long-term debt can be found in Note 3 on page 72 of this report.

Economic Factors and Next Year's Budgets and Rates

- The FY2004-05 Budget Recommendation was submitted at a time when economic conditions were improving and corporate earnings were moving in the right direction.
- The unemployment rate for Lenawee County for June is 7.8 percent, which is a decrease from a rate of 8.4 percent a year ago. This compares with the State's average unemployment rate of 6.4 percent and the national average rate of 5.6 percent.
- Inflationary trends in the region compare favorably with national indices.

All of these factors were considered in preparing the City of Adrian's budget for the 2004-05 fiscal year. Also during the current fiscal year, unreserved fund balance in the General Fund increased by \$721,421 to \$6,309,600 (equivalent to 6.8 months expenditures at current spending levels), due primarily to a change in accounting approach that moved specific items (e.g., City Hall Renovations - \$950,000) from Carryforwards in the Reserved category of Fund Balance to the Designated category of Unreserved Fund Balance. The City of Adrian has appropriated \$576,518 of the Unrestricted Fund Balance amount for spending in the 2004-05 fiscal year budget. It is intended that the use of available fund balance will avoid the need to raise taxes for General Fund operations.

Water and Sewer Rates are anticipated to increase, reflecting the need to fund increased debt service for infrastructure improvements to both systems, as well as compensating for the anticipated sales volume decrease attributable to Madison Township's construction of a redundant waste water treatment system that will divert flows from the Gus Harrison State Correctional Facility.

Requests for Information

This financial report is designed to provide a general overview of the City of Adrian's finances for all those with an interest in the City's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Office of the Finance Director, 100 E. Church Street, Adrian, Michigan 49221 or call 517-264-4824.

city of
ADRIAN

CITY OF ADRIAN, MICHIGAN

STATEMENT OF NET ASSETS

June 30, 2004
With Comparative Totals for June 30, 2003

	<u>PRIMARY GOVERNMENT</u>			<u>COMPONENT UNITS</u>		
	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Totals</u>	<u>Downtown Development Authority</u>	<u>Local Development Finance Authority</u>	
ASSETS:						
Cash and cash equivalents	\$ 2,122,712	\$ 1,626,369	\$ 3,749,081	\$ 4,566,063	\$ 587,270	\$ 46,916
Investments	7,900,638	2,446,051	10,346,689	10,337,928	83,653	
Receivables (net of allowance for uncollectibles)	703,600	1,082,762	1,786,362	2,059,476		
Due from component units	816		816	323		
Due from other governments	335,513	55,580	391,093	383,430		
Internal balances	138,278	(138,278)				
Inventories	131,004	115,995	246,999	231,030		
Prepaid expense	35,536	12,764	48,300	51,288		
Restricted assets:						
Temporarily restricted:						
Cash and cash equivalents		66,688	66,688	68,949		
Investments		1,458,982	1,458,982	1,248,302		
DWRF Bond receivable		217,025	217,025	2,735,260		
Permanently restricted:						
Cash and cash equivalents	42,206		42,206	24,535		
Investments	908,276		908,276	895,519		
Capital Assets (Net of accumulated depreciation):						
Land	7,510,774	904,592	8,415,366	8,415,366		
Land improvements	5,590,458	1,266,207	6,856,665	6,505,677	788,494	
Buildings	2,053,529		2,053,529	2,125,053		
Utility systems		22,664,551	22,664,551	22,665,173		800,400
Machinery, equipment, and furnishings	4,949,753	254,195	5,203,948	5,860,123		
Infrastructure	5,467,545		5,467,545	5,443,658		
Construction in progress		16,182,980	16,182,980	8,480,751		
Total assets	<u>\$ 37,890,638</u>	<u>\$ 48,216,463</u>	<u>\$ 86,107,101</u>	<u>\$ 82,097,904</u>	<u>\$ 1,459,417</u>	<u>\$ 847,316</u>

	<u>PRIMARY GOVERNMENT</u>			<u>COMPONENT UNITS</u>		
	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Totals</u>	<u>Downtown Development Authority</u>	<u>Local Development Finance Authority</u>	
LIABILITIES:						
Accounts payable and other current liabilities	\$ 281,273	\$ 101,794	\$ 383,067	\$ 5,625	\$	
Accrued interest payable	78,673		78,673	55,815		81,700
Due to primary government				816		
Due to other governments		5,427	5,427			
Unearned revenue	44,883		44,883			
Liabilities paid from restricted assets		109,409	109,409			
Noncurrent liabilities:						
Due within one year	377,268	763,387	1,140,655	90,000		
Due in more than one year	1,743,083	14,277,204	16,020,287	575,000		764,100
Total liabilities	2,525,180	15,257,221	17,782,401	727,256		845,800
NET ASSETS:						
Invested in capital assets, net						
related debt	23,761,251	26,559,550	50,320,801	\$ 123,494	\$	36,300
Restricted for:						
Public safety	146,666		146,666			
Community/economic development	824,469		824,469			
Highways and streets	2,674,229		2,674,229			
Debt service		1,505,243	1,505,243			
Endowment	198,898		198,898			
Perpetual care	759,083		759,083			
Other purposes	144,485		144,485			
Unrestricted	6,856,377	4,894,449	11,750,826	608,667		(34,784)
Total net assets	\$ 35,365,458	\$ 32,959,242	\$ 68,324,700	\$ 732,161	\$	1,516

The notes to the financial statements are an integral part of this statement.

(PAGE 1 OF 2)
CITY OF ADRIAN, MICHIGAN

STATEMENT OF ACTIVITIES

For Fiscal Year Ended June 30, 2004
With Comparative Totals for Fiscal Year Ended June 30, 2003

	PROGRAM REVENUES			
	<u>Expenses</u>	<u>Charges For Services</u>	<u>Operating Grants And Contributions</u>	<u>Capital Grants And Contributions</u>
Functions/Programs				
Primary Government:				
Governmental activities:				
General government	\$ 1,684,439	\$ 395,718	\$ 66,015	\$
Public safety	4,601,589	286,899		
Public works	1,076,086	1,877		
Culture and recreation	1,915,082	474,626	679,572	
Other services	1,985,445	291,274	602,640	
Community/economic development	619,075	386,548	127,000	78,597
Highways, streets, and bridges	2,212,509	174,267		237,307
Interest on long term debt	<u>78,673</u>			
Total governmental activities	<u>14,172,898</u>	<u>2,011,209</u>	<u>1,475,227</u>	<u>315,904</u>
Business-type Activities:				
Wastewater system	2,804,095	2,543,309		
Water system	2,425,881	2,773,621		
Dial-A-Ride system	440,192	62,691	205,471	50,111
Automobile parking system	112,969	111,815		
Storm water utility	<u>207,851</u>	<u>263,965</u>		
Total business-type activities	<u>5,990,988</u>	<u>5,755,401</u>	<u>205,471</u>	<u>50,111</u>
Total primary government	<u>\$ 20,163,886</u>	<u>\$ 7,766,610</u>	<u>\$ 1,680,698</u>	<u>\$ 366,015</u>
Component Units:				
Downtown Development Authority	\$ 202,196	\$	\$	\$
Local Development Finance Authority	<u>98,826</u>			
Total component units	<u>\$ 301,022</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
General Revenues:				
Property taxes				
Sales tax				
Motor vehicle fuel tax				
Grants and contributions not restricted to specific programs				
Unrestricted investment earnings				
Transfers				
Total general revenues and transfers				
Change in net assets				
Net assets – beginning of year				
Net assets – end of year				

The notes to the financial statements are an integral part of this statement.

(PAGE 2 OF 2)
CITY OF ADRIAN, MICHIGAN

STATEMENT OF ACTIVITIES

For Fiscal Year Ended June 30, 2004
With Comparative Totals for Fiscal Year Ended June 30, 2003

NET (EXPENSE) REVENUE AND CHANGES IN NET ASSETS					
PRIMARY GOVERNMENT				COMPONENT UNITS	
Governmental Activities	Business-type Activities	Totals 2004	2003	Downtown Development Authority	Local Development Finance Authority
\$ (1,288,721)	\$	\$ (1,288,721)	\$ (1,629,766)	\$	\$
(4,248,675)		(4,248,675)	(3,763,299)		
(1,074,209)		(1,074,209)	(918,339)		
(760,884)		(760,884)	(1,235,699)		
(1,091,531)		(1,091,531)	(392,928)		
(26,930)		(26,930)	108,505		
(1,800,935)		(1,800,935)	(1,605,519)		
(78,673)		(78,673)	(87,538)		
(10,370,558)	-	(10,370,558)	(9,524,583)	-	-
	(260,786)	(260,786)	(329,521)		
	347,740	347,740	190,638		
	(121,919)	(121,919)	(46,865)		
	(1,154)	(1,154)	(2,991)		
	56,114	56,114	87,578		
-	19,995	19,995	(101,161)	-	-
<u>\$ (10,370,558)</u>	<u>\$ 19,995</u>	<u>\$ (10,350,563)</u>	<u>\$ (9,625,744)</u>	<u>\$ -</u>	<u>\$ -</u>
\$	\$	\$	\$	\$ (202,196)	\$
					(98,826)
<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (202,196)</u>	<u>\$ (98,826)</u>
\$ 6,041,046	\$	\$ 6,041,046	\$ 5,914,288	\$ 317,575	\$ 92,126
2,551,255		2,551,255	2,621,990		
1,337,898		1,337,898	1,227,987		
23,008		23,008	660,115		
170,879	95,723	266,602	367,063	5,383	228
(169,127)	169,127				
9,954,959	264,850	10,219,809	10,791,443	322,958	92,354
(415,599)	284,845	(130,754)	1,165,699	120,762	(6,472)
35,781,057	32,674,397	68,455,454	67,289,755	611,399	7,988
<u>\$ 35,365,458</u>	<u>\$ 32,959,242</u>	<u>\$ 68,324,700</u>	<u>\$ 68,455,454</u>	<u>\$ 732,161</u>	<u>\$ 1,516</u>

CITY OF ADRIAN, MICHIGAN

BALANCE SHEET

GOVERNMENTAL FUNDS

June 30, 2004
With Comparative Totals for June 30, 2003

ASSETS	General	Major Streets	Local Streets	Fee And Public-Purpose	Other Governmental Funds	Totals	
						2004	2003
Cash and cash equivalents	\$ 2,224	\$ 827,689	\$ 228,442	\$ 12,661	\$ 1,093,902	\$ 2,164,918	\$ 2,924,124
Investments at cost	6,551,044	1,205,042		144,552	908,276	8,808,914	8,329,185
Receivables:							
Accounts	45,665	11,192		217,718	164,637	439,212	439,807
Loans					256,888	256,888	369,292
Due from other funds	502,571		512,988		47,084	1,062,643	579,510
Due from component units	816					816	323
Due from other governments	335,513					335,513	324,985
Inventories:							
Land held for resale, at cost					7,499	7,499	7,499
Supplies at cost	123,505				123,505	123,505	116,006
Prepaid cost	35,536					35,536	39,883
Total assets	\$ 7,596,874	\$ 2,043,923	\$ 741,430	\$ 374,931	\$ 2,478,286	\$ 13,235,444	\$ 13,130,614
LIABILITIES AND FUND BALANCE							
Liabilities:							
Vouchers payable	\$ 100,679	\$ 3,606	\$ 2,549	\$	\$ 11,019	\$ 117,853	\$ 329,339
Accrued liabilities	159,199	418	1,139		2,664	163,420	126,167
Due to other funds	66,037	27,708	82,428	219,429	528,763	924,365	460,895
Unearned revenue	33,866			11,017		44,883	34,258
Total liabilities	359,781	31,732	86,116	230,446	542,446	1,250,521	950,659
Fund Balances:							
Reserved For:							
Perpetual care					751,584	751,584	721,745
Endowment					198,898	198,898	198,309
Loans					256,888	256,888	369,292
Inventories and prepayments	159,041				7,499	166,540	155,888
Encumbrances	768,452	480,034	304,614	8,878	1,561,978	2,292,109	2,292,109
Unreserved, Reported In:							
General Fund – Designated	4,516,268				4,516,268	4,516,268	5,588,179
General Fund – Undesignated	1,793,332				1,793,332	1,793,332	2,854,433
Special Revenue Funds – Undesignated					712,093	2,739,435	
Total fund balances	7,237,093	1,532,157	350,700	144,485	1,935,840	11,984,923	12,179,955
Total liabilities and fund balance	\$ 7,596,874	\$ 2,043,923	\$ 741,430	\$ 374,931	\$ 2,478,286	\$ 13,235,444	\$ 13,130,614

The notes to the financial statements are an integral part of this statement.

CITY OF ADRIAN, MICHIGAN

**RECONCILIATIONS OF THE BALANCE SHEET OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF NET ASSETS**

For the Fiscal Years Ended June 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Amounts reported for governmental activities in the Statement of Net Assets (page 34) are different because:		
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds.	\$ 25,572,059	\$ 26,051,232
Personal property taxes receivable are not expected to be collected in the current period and, therefore, deferred in governmental funds (presented net of allowance for uncollectibles).	7,500	5,500
Accrued interest payable on long term debt is recognized in governmental funds when paid and not when accrued.	(78,673)	(87,538)
Long-term portion of accrued sick and vacation pay liability are not due and payable in the current period and, therefore, are not reported in the governmental funds.	(309,543)	(367,701)
Bond and loan indebtedness are recognized in the governmental funds when paid and not when accrued.	<u>(1,810,808)</u>	<u>(2,000,391)</u>
Net differences	23,380,535	23,601,102
Total fund balance in governmental funds (page 37)	<u>11,984,923</u>	<u>12,179,955</u>
Total net assets of governmental activities	<u>\$ 35,365,458</u>	<u>\$ 35,781,057</u>

CITY OF ADRIAN, MICHIGAN

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES

GOVERNMENTAL FUNDS

For Fiscal Year Ended June 30, 2004
With Comparative Totals for Fiscal Year Ended June 30, 2003

	General	Major Streets	Local Streets	Fee And Public-Purpose	Other Governmental Funds	Totals Governmental Funds
					2004	2003
Revenues:						
Taxes	\$ 5,573,100	\$	\$	\$	\$ 5,964,834	\$ 5,843,118
Other tax related revenue	74,212				74,212	70,670
Licenses and permits	184,207				184,207	280,389
Intergovernmental – Federal	10,548				89,145	800,346
Intergovernmental – State	2,597,031	1,053,262	338,642		3,988,935	4,160,844
Charges for services	65,345				65,345	66,458
Use and admission charges	314,117				314,117	301,299
Fines and fees	326,021				326,021	275,172
Investment earnings	119,231	13,317		800	170,879	286,010
Fee Trust – for beautification purposes			227,307	1,282,212	1,282,212	1,415,214
Other	493,780	91	130,170		1,322,348	1,262,351
Special assessments					130,170	246,409
Total revenues	9,757,592	1,066,670	696,119	1,283,012	13,912,425	15,008,280
Expenditures:						
Current:						
General government	1,751,826			20,346	1,772,172	1,822,635
Public safety	4,480,272				4,544,000	4,533,808
Public works	912,372				912,372	904,533
Culture and recreation	2,272,317				2,272,317	2,232,404
Other services	1,412,403			101	1,412,504	2,782,935
Community/Economic Development		880,922	1,263,522	615,400	615,400	1,424,600
Highways, streets, and bridges					2,144,444	1,226,250
Debt Service:						
Principal retirement	189,583				189,583	83,253
Interest and fiscal charges	87,538				87,538	49,629
Total expenditures	11,106,311	880,922	1,263,522	20,346	13,950,330	15,060,047
Excess (deficiency) of revenues over (under) expenditures	(1,348,719)	185,748	(567,403)	1,262,666	(37,905)	(51,767)
Other financing sources (uses):						
Transfers in	1,336,251		978,018		2,364,135	1,888,272
Transfers out	(218,993)	(77,030)		(1,282,211)	(2,521,262)	(1,988,705)
Loan proceeds						1,200,000
Total other financing sources (uses)	1,117,258	(77,030)	978,018	(1,282,211)	(157,127)	1,099,567

	<u>General</u>	<u>Major Streets</u>	<u>Local Streets</u>	<u>Fee And Public-Purpose</u>	<u>Other Governmental Funds</u>	<u>Totals Governmental Funds</u> <u>2004</u>	<u>2003</u>
Net change in fund balance	\$ (231,461)	\$ 108,718	\$ 410,615	\$ (19,545)	\$ (463,359)	\$ (195,032)	\$ 1,047,800
Fund balances at beginning of year	<u>7,468,554</u>	<u>1,903,473</u>	<u>244,699</u>	<u>164,030</u>	<u>2,399,199</u>	<u>12,179,955</u>	<u>11,132,155</u>
Fund balances at end of year	<u>\$ 7,237,093</u>	<u>\$ 2,012,191</u>	<u>\$ 655,314</u>	<u>\$ 144,485</u>	<u>\$ 1,935,840</u>	<u>\$ 11,984,923</u>	<u>\$ 12,179,955</u>

CITY OF ADRIAN, MICHIGAN

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES**

For Fiscal Years Ended June 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Amounts reported for governmental activities in the Statement of Revenues, Expenditures and Changes in Fund Balances (Page 39) are different because:		
Net change in fund balance --	\$ (195,032)	\$ 1,047,800
Government funds report capital outlays as expenditures. However, in the Statement of Activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period. (Total capital outlay \$1,916,905 less total depreciation (\$2,396,078).	(479,173)	1,163,213
Revenue in the Statement of Activities that do not provide current financial resources are not reported as revenue in the governmental funds -- net effect on recognizing accrued personal property taxes.	2,000	500
This issuance of long-term debt (e.g. bonds) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds report the effect of issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the Statement of Activities. This amount is the net effect of these differences in the treatment of long-term debt and related items.		
Debt incurred during current year		(1,200,000)
Less: Principal repayment	<u>189,583</u>	<u>83,253</u>
Net	<u>189,583</u>	<u>(1,116,747)</u>
Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.		
Accrued interest -- net effect	8,865	(37,909)
Accrued long-term sick and vacation -- net effect	<u>58,158</u>	<u>(8,959)</u>
Change in net assets in governmental activities (page 36)	<u>\$ (415,599)</u>	<u>\$ 1,047,898</u>

The notes to the financial statements are an integral part of this statement.

(Page 1 of 3)
CITY OF ADRIAN, MICHIGAN

GENERAL FUND

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE -
BUDGET AND ACTUAL

For Fiscal Year Ended June 30, 2004

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget - Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Revenues:				
Taxes	\$ 5,473,125	\$ 5,725,000	\$ 5,573,100	\$ (151,900)
Other tax related revenue	65,000	65,000	74,212	9,212
Licenses and permits	163,745	182,945	184,207	1,262
Intergovernmental	2,714,950	2,616,360	2,607,579	(8,781)
Charges for services	61,670	62,670	65,345	2,675
Uses and admission charges	326,710	306,410	314,117	7,707
Fines and fees	274,500	330,000	326,021	(3,979)
Investment earnings	200,000	152,000	119,231	(32,769)
Miscellaneous	371,850	524,530	493,780	(30,750)
Total revenues	<u>9,651,550</u>	<u>9,964,915</u>	<u>9,757,592</u>	<u>(207,323)</u>
Expenditures:				
Current:				
General Government:				
City Commission	116,120	121,197	108,907	12,290
City Administrator	209,970	278,470	256,060	22,410
Government - Access Channel	48,700	136,392	60,562	75,830
Election Department	15,250	12,250	9,190	3,060
Finance Department	374,020	356,614	304,264	52,350
City Assessor	127,390	194,114	140,229	53,885
City Attorney	158,515	171,515	157,879	13,636
City Clerk	116,475	111,695	108,560	3,135
Personnel Department	128,320	160,285	150,713	9,572
City Hall	106,400	261,757	153,121	108,636
Cemetery	327,125	303,349	302,341	1,008
Total general government	<u>1,728,285</u>	<u>2,107,638</u>	<u>1,751,826</u>	<u>355,812</u>
Public Safety:				
Police Department	2,659,560	2,783,086	2,706,470	76,616
Fire Department	1,347,875	1,435,634	1,341,747	93,887
Community Development	359,235	426,317	421,134	5,183
Animal Control	23,915	18,915	10,921	7,994
Total public safety	<u>4,390,585</u>	<u>4,663,952</u>	<u>4,480,272</u>	<u>183,680</u>
Total expenditures carried forward	<u>6,118,870</u>	<u>6,771,590</u>	<u>6,232,098</u>	<u>539,492</u>

The notes to the financial statements are an integral part of this statement.

(Page 2 of 3)
CITY OF ADRIAN, MICHIGAN

GENERAL FUND

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE –
BUDGET AND ACTUAL

For Fiscal Year Ended June 30, 2004

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget - Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Total expenditures carried forward	\$ 6,118,870	\$ 6,771,590	\$ 6,232,098	\$ 539,492
Public Works:				
Department of Public Works	164,895	185,895	146,359	39,536
Stores - Central Supply	26,780	35,578	706	34,872
Motor Vehicle Pool	(172,450)	(148,662)	(158,884)	10,222
Sidewalks	40,000	68,048	45,383	22,665
Engineering	162,120	115,344	110,527	4,817
Street Lighting	115,200	115,886	127,568	(11,682)
Waste Collection and Disposal	566,090	630,090	640,713	(10,623)
Total public works	902,635	1,002,179	912,372	89,807
Culture and Recreation:				
Recreation Department	894,110	1,021,674	896,642	125,032
Parks and Forestry Department	747,725	842,334	797,977	44,357
Parks and Forestry – Heritage Park	21,905	21,905	21,439	466
Fee Estate Maintenance	550,920	544,078	556,259	(12,181)
Total culture and recreation	2,214,660	2,429,991	2,272,317	157,674
Other Services:				
Library	626,940	637,177	622,372	14,805
Planning Commission	31,150	55,400	17,309	38,091
Beautification – Parks (Fee)	805,500	805,500	665,760	139,740
Park Capital	30,000	237,035	88,491	148,544
Other Projects	5,070	11,920	18,471	(6,551)
Total other services	1,498,660	1,747,032	1,412,403	334,629
Debt Service:				
Principal	189,583	189,583	189,583	
Interest	87,542	87,542	87,538	4
Total debt service	277,125	277,125	277,121	4
Total expenditures	11,011,950	12,227,917	11,106,311	1,121,606
Excess (deficiency) of revenues over (under) expenditures	(1,360,400)	(2,263,002)	(1,348,719)	914,283

The notes to the financial statements are an integral part of this statement.

(Page 3 of 3)
CITY OF ADRIAN, MICHIGAN

GENERAL FUND

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE –
BUDGET AND ACTUAL

For Fiscal Year Ended June 30, 2004

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget - Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Other financing sources (uses):				
Transfers in	\$ 1,447,860	\$ 1,385,860	\$ 1,336,251	\$ (49,609)
Transfers out	<u>(87,460)</u>	<u>(228,259)</u>	<u>(218,993)</u>	<u>9,266</u>
Total other financing sources (uses)	<u>1,360,400</u>	<u>1,157,601</u>	<u>1,117,258</u>	<u>(40,343)</u>
Net change in fund balance	-	(1,105,401)	(231,461)	873,940
Fund balance at beginning of year	<u>7,468,554</u>	<u>7,468,554</u>	<u>7,468,554</u>	<u>-</u>
Fund balance at end of year	<u>\$ 7,468,554</u>	<u>\$ 6,363,153</u>	<u>\$ 7,237,093</u>	<u>\$ 873,940</u>

The notes to the financial statements are an integral part of this statement.

CITY OF ADRIAN, MICHIGAN

MAJOR STREETS SPECIAL REVENUE FUND

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE –
BUDGET AND ACTUAL**

For Fiscal Year Ended June 30, 2004

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget - Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Revenues:				
Intergovernmental – State	\$ 950,535	\$ 970,535	\$ 1,053,262	\$ 82,727
Investment earnings	19,000	14,000	13,317	(683)
Other	<u>12,765</u>	<u>12,765</u>	<u>91</u>	<u>(12,674)</u>
Total revenues	<u>982,300</u>	<u>997,300</u>	<u>1,066,670</u>	<u>69,370</u>
Expenditures:				
Highways, streets, and bridges:				
Street construction	447,880	932,585	454,347	478,238
Routine maintenance – streets	165,705	121,226	168,964	(47,738)
Routine maintenance – bridges	1,515	1,515		1,515
Maintenance – State trunklines	50,535	60,535	54,799	5,736
Traffic service	100,800	110,800	89,322	21,478
Winter maintenance	94,700	70,700	58,390	12,310
Administration	34,460	24,460	29,849	(5,389)
Non-motorized transportation	<u>9,675</u>	<u>30,714</u>	<u>25,251</u>	<u>5,463</u>
Total expenditures	<u>905,270</u>	<u>1,352,535</u>	<u>880,922</u>	<u>471,613</u>
Excess (deficiency) of revenues over (under) expenditures	77,030	(355,235)	185,748	540,983
Other financing uses:				
Transfers out	<u>(77,030)</u>	<u>(77,030)</u>	<u>(77,030)</u>	<u>-</u>
Net change in fund balance	-	(432,265)	108,718	540,983
Fund balance – beginning of year	<u>1,903,473</u>	<u>1,903,473</u>	<u>1,903,473</u>	<u>-</u>
Fund balance – end of year	<u>\$ 1,903,473</u>	<u>\$ 1,471,208</u>	<u>\$ 2,012,191</u>	<u>\$ 540,983</u>

The notes to the financial statements are an integral part of this statement.

CITY OF ADRIAN, MICHIGAN

LOCAL STREETS SPECIAL REVENUE FUND

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE –
BUDGET AND ACTUAL**

For Fiscal Year Ended June 30, 2004

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget - Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Revenues:				
Intergovernmental – State	\$ 304,000	\$ 304,000	\$ 338,642	\$ 34,642
Special assessment	40,610	106,000	130,170	24,170
Other		170,000	227,307	57,307
Total revenues	<u>344,610</u>	<u>580,000</u>	<u>696,119</u>	<u>116,119</u>
Expenditures:				
Highways, streets, and bridges:				
Street construction	462,185	1,370,379	863,084	507,295
Routine maintenance – streets	222,470	238,470	276,332	(37,862)
Routine maintenance – bridges	930	930		930
Traffic service	12,100	61,100	44,542	16,558
Winter maintenance	58,275	58,275	45,280	12,995
Administration	27,910	27,910	34,284	(6,374)
Total expenditures	<u>783,870</u>	<u>1,757,064</u>	<u>1,263,522</u>	<u>493,542</u>
Excess (deficiency) of revenues over (under) expenditures	(439,260)	(1,177,064)	(567,403)	609,661
Other financing sources:				
Transfers in	<u>439,260</u>	<u>990,018</u>	<u>978,018</u>	<u>(12,000)</u>
Net change in fund balance	-	(187,046)	410,615	597,661
Fund balance – beginning of year	<u>244,699</u>	<u>244,699</u>	<u>244,699</u>	-
Fund balance – end of year	<u>\$ 244,699</u>	<u>\$ 57,653</u>	<u>\$ 655,314</u>	<u>\$ 597,661</u>

The notes to the financial statements are an integral part of this statement.

(PAGE 1 OF 2)
CITY OF ADRIAN, MICHIGAN

STATEMENT OF NET ASSETS
PROPRIETARY FUNDS

June 30, 2004
With Comparative Totals for June 30, 2003

BUSINESS-TYPE ACTIVITIES – ENTERPRISE FUNDS

ASSETS	Wastewater System	Water System	Other Enterprise Funds	Totals Proprietary Funds	
				2004	2003
Current assets:					
Cash and cash equivalents	\$ 414,780	\$ 1,035,893	\$ 175,696	\$ 1,626,369	\$ 1,666,474
Investments	2,311,523	134,528		2,446,051	2,904,262
Receivables:					
Accounts	75,463	434,567		510,030	625,760
Special assessments			481,602	481,602	515,302
Deferred assessments	68,501	22,629		91,130	91,130
Accrued interest					12,685
Due from other funds	182,753	17,563	49,611	249,927	227,845
Due from other governments			55,580	55,580	58,445
Inventories		115,995		115,995	107,525
Prepaid expense	<u>5,269</u>	<u>7,495</u>		<u>12,764</u>	<u>11,405</u>
Total current assets	<u>3,058,289</u>	<u>1,768,670</u>	<u>762,489</u>	<u>5,589,448</u>	<u>6,220,833</u>
Noncurrent assets:					
Restricted cash, cash equivalents, investments, and receivables:					
Customer deposits – cash		13,305		13,305	13,981
Bond reserve – investment		200,000		200,000	200,000
Replacement account – investment	500,000	100,000		600,000	600,000
Bond interest and redemption account – investment	403,622	255,360		658,982	448,302
Bond interest and redemption account – cash			53,383	53,383	54,968
DWRF Bond receivable	<u>217,025</u>			<u>217,025</u>	<u>2,735,260</u>
Total restricted assets	<u>1,120,647</u>	<u>568,665</u>	<u>53,383</u>	<u>1,742,695</u>	<u>4,052,511</u>
Capital assets:					
Land	163,164	102,928	638,500	904,592	904,592
Utility systems	26,194,452	14,919,018	2,380,243	43,493,713	42,537,477
Land improvements			1,582,008	1,582,008	1,582,008
Equipment			664,021	664,021	613,910
Less: Accumulated depreciation	(13,080,566)	(6,612,346)	(1,861,877)	(21,554,789)	(20,530,569)
Construction in progress	<u>9,521,316</u>	<u>6,661,664</u>		<u>16,182,980</u>	<u>8,337,151</u>
Net capital assets	<u>22,798,366</u>	<u>15,071,264</u>	<u>3,402,895</u>	<u>41,272,525</u>	<u>33,444,569</u>
Total noncurrent assets	<u>23,919,013</u>	<u>15,639,929</u>	<u>3,456,278</u>	<u>43,015,220</u>	<u>37,497,080</u>
Total assets	<u>\$ 26,977,302</u>	<u>\$ 17,408,599</u>	<u>\$ 4,218,767</u>	<u>\$ 48,604,668</u>	<u>\$ 43,717,913</u>

(PAGE 2 OF 2)
CITY OF ADRIAN, MICHIGAN

STATEMENT OF NET ASSETS
PROPRIETARY FUNDS

June 30, 2004
With Comparative Totals for June 30, 2003

BUSINESS TYPE ACTIVITIES – ENTERPRISE FUNDS

LIABILITIES	Wastewater System	Water System	Other Enterprise Funds	Totals Proprietary Funds 2004	2003
Current liabilities:					
Vouchers payable	\$ 38,309	\$ 45,706	\$ 7,562	\$ 91,577	\$ 1,946,456
Accrued liabilities	1,523	6,166	2,527	10,216	40,285
Due to other funds	40,711	219,365	128,129	388,205	346,460
Due to other governments			5,427	5,427	4,522
General obligation bonds payable – current			145,000	145,000	140,000
Revenue bonds payable – current					250,000
DWRF bonds payable – current	<u>350,000</u>	<u>220,000</u>	<u> </u>	<u>570,000</u>	<u> </u>
Total current liabilities	<u>430,543</u>	<u>491,237</u>	<u>288,645</u>	<u>1,210,425</u>	<u>2,727,723</u>
Current liabilities payable from restricted assets:					
Customer deposits payable		13,305		13,305	13,981
Accrued interest	<u>53,622</u>	<u>35,360</u>	<u>7,122</u>	<u>96,104</u>	<u>11,781</u>
Total current liabilities payable from restricted assets	<u>53,622</u>	<u>48,665</u>	<u>7,122</u>	<u>109,409</u>	<u>25,762</u>
Noncurrent liabilities:					
Accrued sick and vacation pay	44,919	65,673		110,592	147,474
General obligation bonds			200,000	200,000	345,000
DWRF Bonds	<u>8,570,000</u>	<u>5,445,000</u>	<u> </u>	<u>14,015,000</u>	<u>7,797,557</u>
Total noncurrent liabilities	<u>8,614,919</u>	<u>5,510,673</u>	<u>200,000</u>	<u>14,325,592</u>	<u>8,290,031</u>
Total liabilities	<u>9,099,084</u>	<u>6,050,575</u>	<u>495,767</u>	<u>15,645,426</u>	<u>11,043,516</u>
NET ASSETS					
Invested in capital assets, net of related debt	14,095,391	9,416,264	3,057,895	26,559,550	27,647,272
Restricted for debt service	403,622	455,360	46,261	905,243	695,005
Restricted for replacement	500,000	100,000		600,000	600,000
Unrestricted	<u>2,879,205</u>	<u>1,396,400</u>	<u>618,844</u>	<u>4,894,449</u>	<u>3,732,120</u>
Total net assets	<u>\$ 17,878,218</u>	<u>\$ 11,368,024</u>	<u>\$ 3,723,000</u>	<u>\$ 32,959,242</u>	<u>\$ 32,674,397</u>

The notes to the financial statements are an integral part of this statement.

CITY OF ADRIAN, MICHIGAN

**STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS**

**For Fiscal Year Ended June 30, 2004
With Comparative Totals for Fiscal Year Ended June 30, 2003**

BUSINESS-TYPE ACTIVITIES – ENTERPRISE FUNDS

	<u>Wastewater System</u>	<u>Water System</u>	<u>Other Enterprise Funds</u>	Totals Proprietary Funds <u>2004</u>	<u>2003</u>
Operating revenues:					
Charges for services	\$ 2,476,467	\$ 2,510,828	\$ 438,471	\$ 5,425,766	\$ 5,149,863
Miscellaneous revenues	<u>66,842</u>	<u>262,793</u>		<u>329,635</u>	<u>279,266</u>
Total operating revenues	<u>2,543,309</u>	<u>2,773,621</u>	<u>438,471</u>	<u>5,755,401</u>	<u>5,429,129</u>
Operating expenses:					
Cost of services	2,142,717	2,093,464	631,881	4,868,062	4,932,864
Depreciation	<u>607,756</u>	<u>308,072</u>	<u>108,391</u>	<u>1,024,219</u>	<u>985,366</u>
Total operating expenses	<u>2,750,473</u>	<u>2,401,536</u>	<u>740,272</u>	<u>5,892,281</u>	<u>5,918,230</u>
Operating income (loss)	<u>(207,164)</u>	<u>372,085</u>	<u>(301,801)</u>	<u>(136,880)</u>	<u>(489,101)</u>
Nonoperating revenues (expenses):					
Intergovernmental – State			162,797	162,797	168,195
Intergovernmental – Federal			42,674	42,674	40,736
Interest revenue	12,736	55,203	27,784	95,723	118,529
Interest expense	(53,622)	(23,845)	(20,740)	(98,207)	(66,024)
Bond agent expense		(500)		(500)	(250)
Total nonoperating revenues (expenses)	<u>(40,886)</u>	<u>30,858</u>	<u>212,515</u>	<u>202,487</u>	<u>261,186</u>
Income (loss) before contributions and transactions	(248,050)	402,943	(89,286)	65,607	(227,915)
Capital contribution			50,111	50,111	245,283
Transfers in			<u>169,127</u>	<u>169,127</u>	<u>100,433</u>
Change in net assets	(248,050)	402,943	129,952	284,845	117,801
Total net assets – beginning of year	<u>18,126,268</u>	<u>10,955,081</u>	<u>3,593,048</u>	<u>32,674,397</u>	<u>32,556,596</u>
Total net assets – end of year	<u>\$ 17,878,218</u>	<u>\$ 11,358,024</u>	<u>\$ 3,723,000</u>	<u>\$ 32,959,242</u>	<u>\$ 32,674,397</u>

The notes to the financial statements are an integral part of this statement.

(PAGE 1 OF 2)
CITY OF ADRIAN, MICHIGAN

STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS

For Fiscal Year Ended June 30, 2004
With Comparative Totals for Fiscal Year Ended June 30, 2003

INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS

	<u>BUSINESS-TYPE ACTIVITIES – ENTERPRISE FUNDS</u>				
	<u>Wastewater System</u>	<u>Water System</u>	<u>Other Enterprise Funds</u>	Totals <u>Proprietary Funds</u> <u>2004</u>	<u>2003</u>
Cash flows from operating activities:					
Cash received from customers	\$ 2,590,756	\$ 2,868,757	\$ 388,860	\$ 5,848,373	\$ 5,355,412
Cash paid to suppliers	(2,474,719)	(1,992,236)	(313,023)	(4,779,978)	(1,356,108)
Cash paid to employees	<u>(738,633)</u>	<u>(980,171)</u>	<u>(309,810)</u>	<u>(2,028,614)</u>	<u>(1,800,107)</u>
Net cash provided by (used in) operating activities	<u>(622,596)</u>	<u>(103,650)</u>	<u>(233,973)</u>	<u>(960,219)</u>	<u>2,199,197</u>
Cash flows from noncapital financing activities:					
Grant received – Federal			41,566	41,566	38,957
Grant received – State			166,770	166,770	164,658
Transfers from General Fund			<u>167,409</u>	<u>167,409</u>	<u>101,886</u>
Net cash provided by noncapital financing activities	<u>-</u>	<u>-</u>	<u>375,745</u>	<u>375,745</u>	<u>305,501</u>
Cash flows from capital and related financing activities:					
Acquisition and construction of capital assets	(5,181,075)	(3,385,850)		(8,566,925)	(7,654,003)
Principal paid on general obligation bonds			(140,000)	(140,000)	(135,000)
Interest paid and agent fees on general obligation bonds			(21,883)	(21,883)	(28,364)
Special assessments			153,424	153,424	267,840
Special assessment revenue provided to other funds			(66,484)	(66,484)	(396,751)
Principal paid on revenue bonds		(250,000)		(250,000)	(225,000)
Interest paid and agent fees on revenue bonds		(7,031)		(7,031)	(30,749)
Interest paid on DWRP Bonds	(130,479)	(90,131)		(220,610)	(13,522)
Bond proceeds	5,609,725	3,695,953		9,305,678	5,062,297
Contributed capital					<u>150,341</u>
Net cash used in capital and related financing activities	<u>298,171</u>	<u>(37,059)</u>	<u>(74,943)</u>	<u>186,169</u>	<u>(3,002,911)</u>
Cash flows from investing activities:					
Investment securities purchased	(5,878,222)	(2,511,211)		(8,389,433)	(8,145,761)
Proceeds on matured investment securities	5,820,591	2,816,373		8,636,964	8,364,506
Interest income	<u>22,062</u>	<u>58,562</u>	<u>27,784</u>	<u>108,408</u>	<u>126,927</u>
Net cash provided by investing activities	<u>(35,569)</u>	<u>363,724</u>	<u>27,784</u>	<u>355,939</u>	<u>345,672</u>
Net increase (decrease) in cash and cash equivalents	(359,994)	223,015	94,613	(42,366)	(152,541)
Cash and cash equivalents at beginning of year	<u>774,774</u>	<u>826,183</u>	<u>134,466</u>	<u>1,735,423</u>	<u>1,887,964</u>
Cash and cash equivalents at end of year	<u>\$ 414,780</u>	<u>\$ 1,049,198</u>	<u>\$ 229,079</u>	<u>\$ 1,693,057</u>	<u>\$ 1,735,423</u>

NOTE: Noncash items – change in fair value of investments –

Wastewater System	\$ 5,653
Water System	<u>2,157</u>
	<u>\$ 7,810</u>

The notes to the financial statements are an integral part of this statement.

(PAGE 2 OF 2)
CITY OF ADRIAN, MICHIGAN

STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS

For Fiscal Year Ended June 30, 2004
With Comparative Totals for Fiscal Year Ended June 30, 2004

RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH
PROVIDED BY (USED IN) OPERATING ACTIVITIES

	<u>BUSINESS-TYPE ACTIVITIES – ENTERPRISE FUNDS</u>				
	<u>Wastewater System</u>	<u>Water System</u>	<u>Other Enterprise Funds</u>	<u>Totals Proprietary Funds</u>	
				<u>2004</u>	<u>2003</u>
Cash flows from operating activities:					
Operating income (loss)	\$ (207,164)	\$ 372,085	\$ (301,801)	\$ (136,880)	\$ (489,101)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:					
Depreciation	607,756	308,072	108,391	1,024,219	985,366
Change in Assets and Liabilities:					
(Increase) decrease in accounts receivable	21,767	93,963		115,730	(20,374)
(Increase) decrease in due from other funds	25,680	1,849	(49,611)	(22,082)	(53,928)
(Increase) decrease in inventories		(8,470)		(8,470)	14,638
(Increase) in prepaid expense	(1,038)	(321)		(1,359)	(2,176)
Increase (decrease) in vouchers payable	(1,028,494)	(820,839)	(5,545)	(1,854,878)	1,712,436
Increase (decrease) in due to County			905	905	910
Increase (decrease) in accrued payroll and liabilities	(18,110)	(13,529)	1,570	(30,069)	(4,913)
Increase (decrease) in due to other funds	824	(22,719)	12,118	(9,777)	38,897
Increase (decrease) in accrued sick and vacation	(23,817)	(13,065)		(36,882)	16,857
Increase (decrease) in customer deposits		(676)		(676)	585
Total adjustments	<u>(415,432)</u>	<u>(475,735)</u>	<u>67,828</u>	<u>(823,339)</u>	<u>2,688,298</u>
Net cash provided by (used in) operating activities	<u>\$ (622,596)</u>	<u>\$ (103,650)</u>	<u>\$ (233,973)</u>	<u>\$ (960,219)</u>	<u>\$ 2,199,197</u>

The notes to the financial statements are an integral part of this statement.

CITY OF ADRIAN, MICHIGAN
STATEMENT OF FIDUCIARY ASSETS AND LIABILITIES
AGENCY FUNDS

June 30, 2004 and 2003

<u>ASSETS</u>	<u>2004</u>	<u>2003</u>
Cash and cash equivalents	\$ 426,807	\$ 362,161
Total assets	<u>\$ 426,807</u>	<u>\$ 362,161</u>
 <u>LIABILITIES</u>		
Liabilities:		
Vouchers payable	\$ 10,608	\$ 17,350
Restricted deposits	271,886	216,006
Due to other taxing units	<u>144,313</u>	<u>128,805</u>
Total liabilities	<u>\$ 426,807</u>	<u>\$ 362,161</u>

The notes to the financial statements are an integral part of this statement.

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the City of Adrian, Michigan have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the government's accounting policies are described below:

A. Reporting Entity

The City of Adrian is a Michigan Municipal Corporation governed by an elected seven member commission. The accompanying financial statements present the government and its component units, entities for which the government is considered to be financially accountable. Blended component units, although legally separate entities, are, in substance, part of the government's operations. Each discretely presented component unit is reported in a separate column in the government-wide financial statements (see note below for description) to emphasize that it is legally separate from the government.

Blended component unit. The City of Adrian Building Authority is governed by a three member board appointed by the City Commission. Although it is legally separate from the City, the City of Adrian Building Authority is reported as if it was part of the primary government because its sole purpose is to finance the construction of City parking lots.

The City of Adrian Building Authority is reported in the financial statements as part of the 'Automobile Parking System Enterprise Fund', where the revenues of the fund are paying off the bond issue of the Authority.

Discretely presented component units.

Downtown Development Authority (DDA) was created as a separate legal entity under Public Act 197 of 1975 of the State of Michigan. The purpose of the DDA is to plan and develop the downtown area of the City and to attract new businesses and residents. The governing body of DDA is appointed by the City Commission for a fixed term. The City approves the annual budget and any capital projects of DDA. Prior approval by the City is needed on any taxation by DDA. And, the City's approval is needed for any borrowing done by DDA. The Downtown Development Authority is presented as a governmental fund type.

The other discretely presented component unit is the Local Development Finance Authority (LDFA) created under Public Act 281 of 1986 of the State of Michigan. The LDFA's purpose is to work toward the elimination of the causes of unemployment, underemployment and joblessness, and to promote economic growth in the City of Adrian. The City appoints the majority of the LDFA Board of Directors. The budget of the LDFA needs the City's approval. And, the main revenue source of LDFA which is tax increment financing is a financial burden to the City. The Local Development Finance Authority is presented as a governmental fund type.

Separate financial statements for each of the individual component units are not available.

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS

June 30, 2004

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Government-wide and fund financial statements

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the nonfiduciary activities of the primary government and its component units. For the most part, the effect of interfund activity has been removed from these statements. *Governmental activities*, which normally are supported by taxes and intergovernmental revenues, are reported separately from *business-type activities*, which rely to a significant extent on fees and charges for support. Likewise, the *primary government* is reported separately from certain legally separate *component units* for which the primary government is financially accountable.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function or segment. *Program revenues* include 1) charges to customers or applicants who purchase, use or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as *general revenues*.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

C. Measurement focus, basis of accounting and financial statement presentation

The government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*, as are the proprietary fund and fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures are recorded only when payment is due.

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Amounts due from other governments, loans receivable, Fee funding, and services provided associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the government.

The government reports the following major governmental funds:

The *General Fund* is the government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in an other fund.

The *Major Streets Fund* is a Special Revenue Fund that receives State and local funding for the purpose of construction and maintenance of City streets designated as major streets under State of Michigan Act 51 of Public Acts of 1951.

The *Local Streets Fund* is a Special Revenue Fund that receives State and local funding for the purpose of construction and maintenance of City streets designated as local streets under State of Michigan Act 51 of Public Acts of 1951.

The *Fee and Public-Purpose Fund* is a Special Revenue Fund that receives funds that are restricted for specific public-purpose uses and can be fully expended for the restricted purpose or purposes.

The government reports the following major proprietary funds.

The *Wastewater System Fund* accounts for the acquisition, operation, and maintenance of the City's wastewater system.

The *Water System Fund* accounts for the acquisition, operation and maintenance of the City's water system.

Additionally, the government reports the following fund types:

The *Agency Funds* account for assets held by the City acting as an agent for individuals, private organizations, other governments, and/or other funds.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the *option* of the following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The City has elected not to follow subsequent private-sector guidance.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are payments of utility charges between the City's water and sewer function and various other functions of the government. Elimination of these charges would distort the direct costs and program revenues reported for the various function concerned.

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS

June 30, 2004

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Amounts reported as *program revenues* included 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as *general revenues* rather than as program revenues. Likewise, general revenues include all taxes.

Proprietary Funds distinguish *operating* revenues and expenses from *nonoperating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the Wastewater and Water Enterprise Funds are charges to customers for sales and services. The Wastewater and Water Enterprise Funds also recognize as operating revenues the portion of tap fees intended to recover the cost of connecting new customers to the system. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the government's policy to use restricted resources first, then unrestricted resources as they are needed.

D. Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

E. Assets, liabilities, and net assets or equity.

1. Cash and investments

Cash includes amounts in cash on hand, demand deposits, as well as short-term investments with a maturity date within three months of the date acquired by the government.

Investments include commercial paper and federal securities.

State statutes authorize the government to invest in Obligations of the U.S. Treasury, Federal Agencies, commercial paper, corporate bonds, repurchase agreements, and State approved Investment Pools.

Investments are stated at fair value. The evaluation of investments is an accounting change. In the past, investments were valued at cost. This change in accounting had only a minimal effect on the financial statements. (See Note 3. A. for effects on funds).

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS

June 30, 2004

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2. Receivables and payables

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the noncurrent portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds." Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances."

Advances between funds, as reported in the fund financial statements, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources. The City had no advances between funds at June 30, 2004.

Personal property taxes receivable is shown net of an allowance for uncollectibles. Based on past history, the majority of personal property taxes receivable are considered uncollectible and reserved in the allowance for uncollectibles.

Property taxes are levied as of July 1 on property values assessed as of the prior December 31. The billing is mailed on July 1 and is considered due upon receipt by the taxpayer; however, the actual due date is August 31. A lien on property occurs when property taxes are levied (July 1). On August 31, the bill becomes delinquent and penalties and interest may be assessed by the government.

Delinquent real property taxes are turned over to the County and reimbursed through a revolving fund. Therefore, property taxes receivable are not accounted for under the 60 day rule.

3. Inventories and prepaid items

All inventories are valued at cost using the first-in/first-out (FIFO) method. Inventories of governmental funds are recorded as expenditures when consumed rather than when purchased.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

4. Restricted assets

Certain proceeds of enterprise fund revenue bonds and general obligations bonds, as well as certain resources set aside for their repayment, are classified as restricted assets on the balance sheet because their use is limited by applicable bond covenants. The bond interest and redemption account is used to segregate resources accumulated for debt service payments. The bond reserve account is used to report resources set aside to make debt service payment on bonds which would otherwise be in default. The replacement account is used to report resources set aside to make major repairs and replacements to fixed operation assets of the enterprise fund.

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS

June 30, 2004

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

5. Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., road, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets are defined by the government as assets with an initial, individual cost of more than \$5,000 (amount not rounded) and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed.

Property, plant, and equipment of the primary government, as well as the component units, are depreciated using the straight line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Land improvements	20 – 50
Buildings	10 – 20
Machinery, equipment, and furnishings	5 – 35
Utility systems	50 – 100
Infrastructure	15 – 100

6. Compensated absences

Vacation leave benefits for City employees are based on past services rendered and are accrued as a liability based on the expected use of the benefits through paid time off and cash payments at termination or retirement. The accrued liability for vacation time is determined under the vesting method as defined by GASB Statement 16.

Sick leave for City employees is vested to the extent that cash payments are made (up to allowable limits) to employees upon retirement. The accrued liability for sick leave is determined under the termination method as defined by GASB Statement 16.

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS

June 30, 2004

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The current portion (the amount normally expected to be liquidated with expendable available financial resources) of accrued sick and vacation pay are shown as a liability and expenditure in the applicable governmental fund types. The entire accrued sick and vacation pay related to governmental fund types is reported in the government-wide statements.

In the proprietary funds as well as in the government-wide statements, the vested sick and vacation pay are recorded as an expense and liability of those funds as the benefits accrue to employees.

7. Long-term obligations

In the governmental-wide financial statements and proprietary fund types in the fund financial statements long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net assets. Bond premiums and discounts, as well as issuance costs, if any, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of any applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognize any bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

8. Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

9. Comparative data/reclassification

Comparative data for the prior year have been presented only for individual enterprise funds in the fund financial statements in order to provide an understanding of the changes in the financial position and operations of these funds. Also, certain amounts presented in the prior year data have been reclassified in order to be consistent with current year's presentation.

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS

June 30, 2004

NOTE 2. STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

A. Budgetary information

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for all governmental funds except the Fee and Public-Purpose Special Revenue Fund and the permanent funds which are not budgeted. All annual appropriations lapse at fiscal year end.

On or before the last Tuesday of February each year, all departments of the City submit requests for appropriations to the Finance Director so that a budget may be prepared. With the first City Commission meeting in April, the proposed budget is presented to the City Commission for review. The Commission holds public hearings and a final budget must be prepared and adopted no later than the second week of May.

The appropriated budget is prepared by fund, function, and activity. The legal level of budgetary control (i.e., the level at which expenditures may not legally exceed appropriations) is with the City Commission. The Commission made several supplemental budgetary appropriations throughout the year, including increases in construction in Major and Local Streets' Funds totaling \$1,392,899. The supplemental budgetary appropriations made in the General Fund were in anticipation of normal activity.

Encumbrance accounting is employed in governmental funds. Encumbrances (e.g., purchase orders, contracts) outstanding at year end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be reappropriated and honored during the subsequent year.

B. Excess of expenditures over appropriations in budgetary funds

P.A. 621 of 1978, Section 18(1), as amended, of the State of Michigan provides that a local governmental unit shall not incur expenditures in excess of the amount appropriated.

In the body of the financial statements, the City's actual expenditures and budgeted expenditures for the budgetary funds have been shown on a functional/activity basis. The approved budgets of the City for these budgetary funds were adopted to the activity level which, in many cases, is the department level.

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS

June 30, 2004

NOTE 2. STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY (Continued)

During the year ended June 30, 2004, the City incurred expenditures in certain budgetary funds which were in excess of the amounts appropriated, as follows:

<u>Fund</u>	<u>Appropriations</u>	<u>Amount of Expenditures</u>	<u>Budget Variance</u>
General Fund			
Street lighting	\$ 115,886	\$ 127,568	\$ 11,682
Waste collection	630,090	640,713	10,623
Fee Estate maintenance	544,078	556,259	12,181
Other projects	11,920	18,471	6,551
Major Streets Fund			
Routine maintenance – streets	121,226	168,964	47,738
Administration	24,460	29,849	5,389
Local Streets Fund			
Routine maintenance – streets	238,470	276,332	37,864
Administration	27,910	34,284	6,374
Community Development Fund			
Community Development	517,227	555,891	38,664
OMNI Fund			
Public Safety	62,000	63,728	1,728

These additional expenditures were funded by greater than anticipated revenues in the case of Major Streets, Local Streets, and OMNI Special Revenue Funds.

C. Fund equity – designations

The City Commission has designated a part of the General Fund's unreserved fund balance for the following purposes:

1.	DPW – Motor Pool – Depreciation Catch-Up	\$ 1,100,000
2.	City Hall Renovations	950,000
3.	Funding for fiscal year 2004-05 Budget	576,518
4.	Parks and Forestry Building	400,000
5.	Technology Infrastructure Upgrades	400,000
6.	Property Acquisitions and Options (Pearl Street, Other)	350,000
7.	Geographic Information System	225,000
8.	Increase in Actuarially Determined Pension Contribution	132,000
9.	Financial System (Including Utility Billing System)	125,000
10.	Street Sweeper	125,000
11.	Technology Training	50,000
12.	Information Technology – Depreciation Catch-Up	31,750
13.	City Clerk/Police Department – Document Imaging System	26,000
14.	Local Grant Match	25,000
		<hr/>
	Total Proposed Designations	<u>\$ 4,516,268</u>

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS

June 30, 2004

NOTE 3. DETAILED NOTES ON ALL FUNDS

A. Deposits and investments

Primary Government

Deposits. At year end, the carrying value of the City's deposits was \$9,806,525 (which includes Agency Fund cash of \$426,807) and the bank balance was \$10,738,061. The total bank balance is classified in the following three categories of credit risk: (1) Insured or collateralized with securities held by the City or by its agent in the City's name. (2) Collateralized with securities held by a pledging financial institution's trust department or agent in the City's name. (3) Uncollateralized. (This includes any bank balance that is collateralized with securities held by a pledging financial institution or by its trust department or agent but not in the City's name.)

Due to higher cash flows during certain times of the year, especially when property taxes are being collected, deposits of the City increase significantly. As a result, the amounts classified in category 3 at those times of year were substantially higher than at year end.

	<u>CATEGORIES</u>			
	<u>1</u>	<u>2</u>	<u>3</u>	<u>Total</u>
Certificates of Deposit	\$ 1,216,139	\$	\$ 1,147,500	\$ 2,363,639
Money Market	400,000		6,171,266	6,571,266
Demand Deposits	<u>100,000</u>	<u></u>	<u>1,703,156</u>	<u>1,803,156</u>
	<u>\$ 1,716,139</u>	<u>\$ -</u>	<u>\$ 9,021,922</u>	<u>\$ 10,738,061</u>

Bank balances shown in Category 1 are insured by Federal Depository Insurance.

All deposits are with banks located in Michigan as required by statutes.

Component Units

Deposits. The component units had deposits with a carrying value of \$717,839 and bank balance of \$720,435 at year end. The credit risk to the bank balance is as follows:

	<u>CATEGORIES</u>			
	<u>1</u>	<u>2</u>	<u>3</u>	<u>Total</u>
Certificates of Deposit	\$ 83,653	\$	\$	\$ 83,653
Demand Deposits	<u>100,000</u>	<u></u>	<u>536,782</u>	<u>636,782</u>
	<u>\$ 183,653</u>	<u>\$ -</u>	<u>\$ 536,782</u>	<u>\$ 720,435</u>

All deposits are with banks located in Michigan as required by statutes.

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS

June 30, 2004

NOTE 3. DETAILED NOTES ON ALL FUNDS (Continued)

Primary Government

Investments. The City's investments are classified in the following three categories of credit risk: (1) Insured or registered, or securities held by the City or its agent in the City's name. (2) Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the City's name. (3) Uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in the City's name.

CATEGORIES

	<u>1</u>	<u>2</u>	<u>3</u>	<u>Fair Value</u>	<u>Cost Value</u>
Federal Agencies' Securities	\$ 6,692,204	\$	\$	\$ 6,692,204	\$ 6,740,287
Commercial Paper	<u>500,000</u>	<u> </u>	<u> </u>	<u>500,000</u>	<u>500,000</u>
Total investments	<u>\$ 7,192,204</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 7,192,204</u>	<u>\$ 7,240,287</u>

The following is a summary of the City's cash and investments at June 30, 2004:

Carrying Value

	<u>Primary Government</u>	<u>Component Units</u>
Cash and Cash Equivalents:		
Checking and savings accounts	\$ 3,857,975	\$ 634,186
Checking and savings accounts – Agency Fund	<u>426,807</u>	<u> </u>
Total cash and cash equivalents	<u>4,284,782</u>	<u>634,186</u>
Investments:		
Savings and money market accounts	1,793,155	83,653
Cash accounts – U.S. Government	1,364,949	
Certificates of deposits with original maturity of more than three months	2,363,639	
Federal Agencies Notes/Bonds	6,692,204	
Commercial paper	<u>500,000</u>	<u> </u>
Total investments	<u>12,713,947</u>	<u>83,653</u>
Total cash, cash equivalents, and investments	<u>\$ 16,998,729</u>	<u>\$ 717,839</u>

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS

June 30, 2004

NOTE 3. DETAILED NOTES ON ALL FUNDS (Continued)

The effect of the change in valuation of investments from cost to fair value on the funds of the City:

<u>Fund</u>	<u>Unrealized Gain or (Loss)</u>
General Fund	\$ (29,548)
Wastewater Fund	(5,653)
Water Fund	(2,157)
Perpetual Care Fund	<u>(10,725)</u>
	<u>\$ (48,083)</u>

The unrealized losses on investments are shown as part of investment earnings in the financial statements.

B. Receivables

Receivables as of year end for the government's individual major and nonmajor funds in the aggregate, including the applicable allowances for uncollectible accounts, are as follows:

	<u>General</u>	<u>Major Streets</u>	<u>Local Streets</u>	<u>Fee And Public- Purpose</u>	<u>Wastewater System</u>	<u>Water System</u>	<u>Nonmajor Funds</u>	<u>Total</u>
Receivables:								
Taxes	\$ 401,372	\$	\$	\$	\$	\$	\$	\$ 401,372
Accounts	45,665	11,192		217,718	75,463	434,567	164,637	949,242
Special assessments					68,501	22,629	481,602	572,732
Intergovernmental	335,513						55,580	391,093
Community Development loans								
							<u>256,888</u>	<u>256,888</u>
Gross receivables	782,550	11,192	-	217,718	143,964	457,196	958,707	2,571,327
Less: Allowance for uncollectibles	<u>(401,372)</u>							<u>(401,372)</u>
Net total receivables	<u>\$ 381,178</u>	<u>\$ 11,192</u>	<u>\$ -</u>	<u>\$ 217,718</u>	<u>\$ 143,964</u>	<u>\$ 457,196</u>	<u>\$ 958,707</u>	<u>\$ 2,169,955</u>

Governmental funds defer revenue recognition in connection with resources that have been received, but not yet earned. At the end of the current fiscal year, the various components of *unearned revenue* reported in the government funds were as follows:

	<u>Unearned Revenue</u>
Funds for training classes to be held in the future	\$ 20,535
Donations restricted for library not yet earned	13,331
Forfeiture funds for police not yet earned	<u>11,017</u>
	<u>\$ 44,883</u>

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

NOTE 3. DETAILED NOTES ON ALL FUNDS (Continued)

C. Capital assets

Capital asset activity for the year ended June 30, 2004 was as follows:

Primary Government

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Governmental activities:				
Capital assets, not being depreciated:				
Land	\$ 7,510,774	\$	\$	\$ 7,510,774
Construction in progress	<u>143,600</u>	<u> </u>	<u>(143,600)</u>	<u> </u>
Total capital assets, not being depreciated	<u>7,654,374</u>	<u>-</u>	<u>(143,600)</u>	<u>7,510,774</u>
Capital assets, being depreciated:				
Land improvements	5,659,179	418,250		6,077,429
Buildings	4,611,364			4,611,364
Machinery, equipment, and furnishings	9,742,512	181,224		9,923,736
Infrastructure	<u>29,476,531</u>	<u>1,461,031</u>	<u> </u>	<u>30,937,562</u>
Total capital assets, being depreciated	<u>49,489,586</u>	<u>2,060,505</u>	<u>-</u>	<u>51,550,091</u>
Less: Accumulated depreciation for:				
Land improvements	(435,235)	(51,736)		(486,971)
Buildings	(2,486,311)	(71,524)		(2,557,835)
Machinery, equipment, and furnishings	(4,138,309)	(835,674)		(4,973,983)
Infrastructure	<u>(24,032,873)</u>	<u>(1,437,144)</u>	<u> </u>	<u>(25,470,017)</u>
Total accumulated depreciation	<u>(31,092,728)</u>	<u>(2,396,078)</u>	<u>-</u>	<u>(33,488,806)</u>
Total capital assets, being depreciated, net	<u>18,396,858</u>	<u>(335,573)</u>	<u>-</u>	<u>18,061,285</u>
Governmental activities, capital assets – net	<u>\$ 26,051,232</u>	<u>\$ (335,573)</u>	<u>\$ (143,600)</u>	<u>\$ 25,572,059</u>

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS

June 30, 2004

NOTE 3. DETAILED NOTES ON ALL FUNDS (Continued)

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Business-type activities:				
Capital assets, not being depreciated:				
Land	\$ 904,592	\$	\$	\$ 904,592
Construction in progress	<u>8,337,151</u>	<u>7,845,829</u>		<u>16,182,980</u>
Total capital assets, not being depreciated	<u>9,241,743</u>	<u>7,845,829</u>	-	<u>17,087,572</u>
Capital assets, being depreciated:				
Land improvements	1,582,008			1,582,008
Utility systems	42,537,477	956,236		43,493,713
Machinery, equipment, and furnishings	<u>613,910</u>	<u>50,111</u>		<u>664,021</u>
Total capital assets, being depreciated	<u>44,733,395</u>	<u>1,006,347</u>	-	<u>45,739,742</u>
Less: Accumulated depreciation for:				
Land improvements	(300,275)	(15,526)		(315,801)
Utility systems	(19,872,304)	(956,858)		(20,829,162)
Machinery, equipment, and furnishings	<u>(357,990)</u>	<u>(51,836)</u>		<u>(409,826)</u>
Total accumulated depreciation	<u>(20,530,569)</u>	<u>(1,024,220)</u>	-	<u>(21,554,789)</u>
Total capital assets, being depreciated – net	<u>24,202,826</u>	<u>(17,873)</u>	-	<u>24,184,953</u>
Business-type activities, capital assets – net	<u>\$ 33,444,569</u>	<u>\$ 7,827,956</u>	<u>\$ -</u>	<u>\$ 41,272,525</u>

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

NOTE 3. DETAILED NOTES ON ALL FUNDS (Continued)

Depreciation expense was charged to functions/programs of the primary government as follows:

Governmental activities:

General government	\$ 56,998
Public safety	117,927
Public works (includes sidewalks and street lights)	166,006
Culture and recreation (includes parks)	91,690
Other services (includes library)	568,707
Community/economic development	6,005
Highways, streets, and bridges	<u>1,388,745</u>

Total depreciation expense – governmental activities	<u>\$ 2,396,078</u>
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Business-type activities:

Wastewater system	\$ 607,757
Water system	308,071
Dial-A-Ride system	50,478
Automobile parking system	16,883
Storm water system	<u>41,030</u>

Total depreciation expense – business-type activities	<u>\$ 1,024,219</u>
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Construction commitments

The government has active construction projects as of June 30, 2004. The projects include street construction and improvements to the wastewater system and the water system. At year end the government's commitments with contractors are as follows:

	<u>Spent-to-Date</u>	<u>Remaining Commitment</u>
Street construction – Major Streets	\$ 35,552	\$ 452,132
Street construction – Local Streets	129,619	311,723
Wastewater system construction	4,806,976	206,343
Water system construction	<u> </u>	<u>94,290</u>
Total	<u>\$ 4,972,147</u>	<u>\$ 1,064,488</u>

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS

June 30, 2004

NOTE 3. DETAILED NOTES ON ALL FUNDS (Continued)

The special assessment portion of the commitment for street construction is being financed by the Capital Project Fund that will be repaid by the benefiting property owners. The City's portion of these projects are being funded by the transfer of existing resources from the Municipal Streets Fund. The commitment for improvements to the wastewater and water systems is being financed by revenue bonds secured by wastewater and water revenues.

Discretely presented component units:

Capital asset activity for the Downtown Development Authority (DDA) for the year ended June 30, 2004 was as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets, not being depreciated:				
Land	\$ 53,494	\$	\$	\$ 53,494
Capital assets, being depreciated:				
Land improvements	1,225,000			1,225,000
Less: Accumulated depreciation for:				
Land improvements	<u>(441,000)</u>	<u>(49,000)</u>	<u></u>	<u>(490,000)</u>
DDA capital assets – net	<u>\$ 837,494</u>	<u>\$ (49,000)</u>	<u>\$ -</u>	<u>\$ 788,494</u>

Capital asset activity for the Local Development Finance Authority (LDFA) for the year ended June 30, 2004 was as follows:

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital assets, being depreciated:				
Utility systems	\$ 920,000	\$	\$	\$ 920,000
Less: Accumulated depreciation for:				
Utility	<u>(110,400)</u>	<u>(9,200)</u>	<u></u>	<u>(119,600)</u>
LDFA capital assets – net	<u>\$ 809,600</u>	<u>\$ (9,200)</u>	<u>\$ -</u>	<u>\$ 800,400</u>

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

NOTE 3. DETAILED NOTES ON ALL FUNDS (Continued)

D. Interfund receivables, payables, and transfers

Primary Government

Due to/from other funds:

<u>Fund</u>	<u>Interfund Receivable</u>	<u>Fund</u>	<u>Interfund Payable</u>
General	\$ 502,571	Capital Projects Revolving	\$ 53,240
		Major Streets	27,708
		Local Streets	52,988
		Community Development	4,559
		Economic Development	6,250
		OMNI	22
		Wastewater System	23,148
		Water System	36,612
		Storm Water Utility	28,998
		Fee And Public-Purpose	219,429
		Endowment Trust	3,436
		Perpetual Care	290
		Dial-A-Ride	45,891
	<u>502,571</u>		<u>502,571</u>
Local Streets	<u>512,988</u>	Municipal Streets	<u>512,988</u>
Community Development	<u>47,084</u>	General	45,866
		Economic Development	1,218
	<u>47,084</u>		<u>47,084</u>
Wastewater System	<u>182,753</u>	Water System	<u>182,753</u>
Storm Water Utility	<u>29,440</u>	Local Streets	<u>29,440</u>
Water System	<u>17,563</u>	Wastewater System	<u>17,563</u>
Auto Parking	<u>20,171</u>	General	<u>20,171</u>
Total primary government	<u>\$ 1,312,570</u>		<u>\$ 1,312,570</u>

Due to/from primary government and component units:

<u>Receivable Entity</u>		<u>Payable Entity</u>	
General (primary government)	<u>\$ 816</u>	Downtown Development Authority (component unit)	<u>\$ 816</u>

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

NOTE 3. DETAILED NOTES ON ALL FUNDS (Continued)

Interfund transfers:

Primary Government

Transfers out:	<u>Transfers In</u>				<u>Total</u>
	<u>General Fund</u>	<u>Local Streets</u>	<u>Nonmajor Government</u>	<u>Nonmajor Enterprise</u>	
General Fund	\$	\$	\$	\$	\$
Major Streets	12,000	65,030	49,866	169,127	218,993
Fee and Public-Purpose	1,282,211				77,030
Nonmajor Governmental	30,040	912,988			1,282,211
	<u>\$ 1,324,251</u>	<u>\$ 978,018</u>	<u>\$ 49,866</u>	<u>\$ 169,127</u>	<u>\$ 2,521,262</u>

E. Long-term debt

General obligation bonds. The government issues general obligation bonds to provide funds for the acquisition and construction of major capital facilities and land purchase. General obligation bonds have been issued for both business-type activities and component unit.

General obligation bonds are direct obligations and pledge the full faith and credit of the government. General obligation bonds currently outstanding are as follows:

<u>Purpose</u>	<u>Date of Issue</u>	<u>Amount of Issue</u>	<u>Interest Rates</u>	<u>Final Maturity Date</u>	<u>Annual Principal Payments</u>	<u>Balance Outstanding</u>
Primary Government						
Business-type activities:						
Auto Parking	9/01/89	\$ 500,000	6.9%	9/01/2004	\$ 50,000	\$ 50,000
Storm Water Utility	1/01/97	800,000	4.5 to 4.8%	9/01/2006	\$ 95,000 to 100,000	295,000
						<u>\$ 345,000</u>
Component Unit						
Downtown Development Authority	10/01/92	\$ 1,025,000	6.4%	3/01/2012	\$ 80,000 to 90,000	<u>\$ 665,000</u>

CITY OF ADRIAN, MICHIGAN
NOTES TO FINANCIAL STATEMENTS
June 30, 2004

NOTE 3. DETAILED NOTES ON ALL FUNDS (Continued)

Primary Government

The City is purchasing a parcel of land, located in Adrian Township, with an installment purchase obligation from the Bank of Lenawee which replaces the original land contract arrangement to purchase the land. The installment purchase is for \$1,000,000 with an interest rate of 5.75% per annum. Payments will be made semiannually over a ten year term. The debt is a general obligation to the City.

The City also has purchased a parcel of land, located in Madison Township, with an installment purchase obligation from the Bank of Lenawee. The installment purchase is for \$1,200,000 with an interest rate of 3.64% per annum. Payments are made semiannually over a ten year term. The debt is a general obligation to the City.

The installment purchase obligations currently outstanding are:

	<u>Closing Date</u>	<u>Value of Contract</u>	<u>Interest</u>	<u>Final Maturity Date</u>	<u>Annual Principal Payments</u>	<u>Balance Outstanding</u>
Governmental:						
Parks and Trees Department	8/1/00	\$ 1,000,000	5.75%	8/01/2010	\$ 64,584 to 123,808	\$ 712,282
Parks and Trees Department	5/23/03	\$ 1,200,000	3.64%	5/23/2013	\$ 105,201 to 140,394	1,098,526
						<u>\$ 1,810,808</u>

Annual debt service requirements to maturity for general obligation bonds and bank loans are as follows:

<u>Year Ending June 30</u>	<u>Governmental Activities</u>		<u>Business-Type Activities</u>		<u>Component Unit – DDA</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2005	\$ 198,448	\$ 78,673	\$ 145,000	\$ 13,410	\$ 90,000	\$ 42,560
2006	207,751	69,369	100,000	7,150	85,000	36,800
2007	217,514	59,607	100,000	2,400	85,000	31,360
2008	227,759	49,363			85,000	25,920
2009	238,512	38,610			80,000	20,480
2010 – 2013	720,824	55,459			240,000	30,720
	<u>\$ 1,810,808</u>	<u>\$ 351,081</u>	<u>\$ 345,000</u>	<u>\$ 22,960</u>	<u>\$ 665,000</u>	<u>\$ 187,840</u>